



Committed to
Long-Term Value Creation

Annual Report 2014



Corporate Philosophy

The Best of Nature and Science

Corporate Mission

To contribute to the unparalleled medical therapeutic power of the combination of Kampo medicine and Western medicine.

Tsumura's Business

Tsumura's core business is the manufacture and sale of prescription Kampo products. As a leading company in the field of Kampo medicine, Tsumura aims to achieve sustainable growth and build its corporate value through the provision of a stable supply of high-quality Kampo products.

GLOSSARY

Kampo Medicine

The medicine traditionally practiced in Japan, based on ancient Chinese medicine.

Crude Drugs

Crude drugs are the main raw materials for Kampo products and primarily indicate the portion of plants and minerals used for medicinal purposes.

Western Medicine

Originating with the practice of medicine in Greece, Western medicine is used as the counterpart to Eastern medicine.

Kampo Business

A business model including not only the production and sale of Kampo products, but also encompassing the cultivation, processing, and storage of crude drugs.

Kampo Medicines

Kampo medicines are used in the practice of Kampo medicine.

"Drug Fostering" Program

A program that aims to build a body of scientific evidence on the efficacy of Kampo products.

Forward-looking Statements

In this annual report, all statements that contain the words "believe," "anticipate," "estimate," "expect," or other similar words, and all numbers related to future performance, are considered forward-looking statements that are not historical facts but rather reflect management's best judgment and the most information available at the time this annual report was prepared. The actual results that Tsumura will achieve in the future may differ greatly from these estimates and forecasts due to various uncertain factors in the business environment and various risks that are discussed later in this annual report. The forward-looking statements contained herein were deemed reasonable by management at the time that we prepared this annual report, but it is important to exercise ample caution when making investment decisions based on these statements.



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"Tsumura is working to implement strategies and attain sustainable growth to achieve its long-term vision."

Along with the business results for fiscal 2014 and a review of progress with the Company's medium-term management plan, the president reports on the long-term outlook for the prescription Kampo product business and measures being taken to enhance corporate value.

15 **Special Feature:**
Tsumura's Commitment to Long-Term Value Creation



The special feature demonstrates Tsumura's commitment to pursuing business development from a long-term perspective through three aspects of its business: establishing a producers' network, accumulating manufacturing technology and know-how, and developing communication channels with physicians.

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38 **Creating Shared Value**



**Shared Value of Crude Drug
Procurement and Agricultural Vitalization**

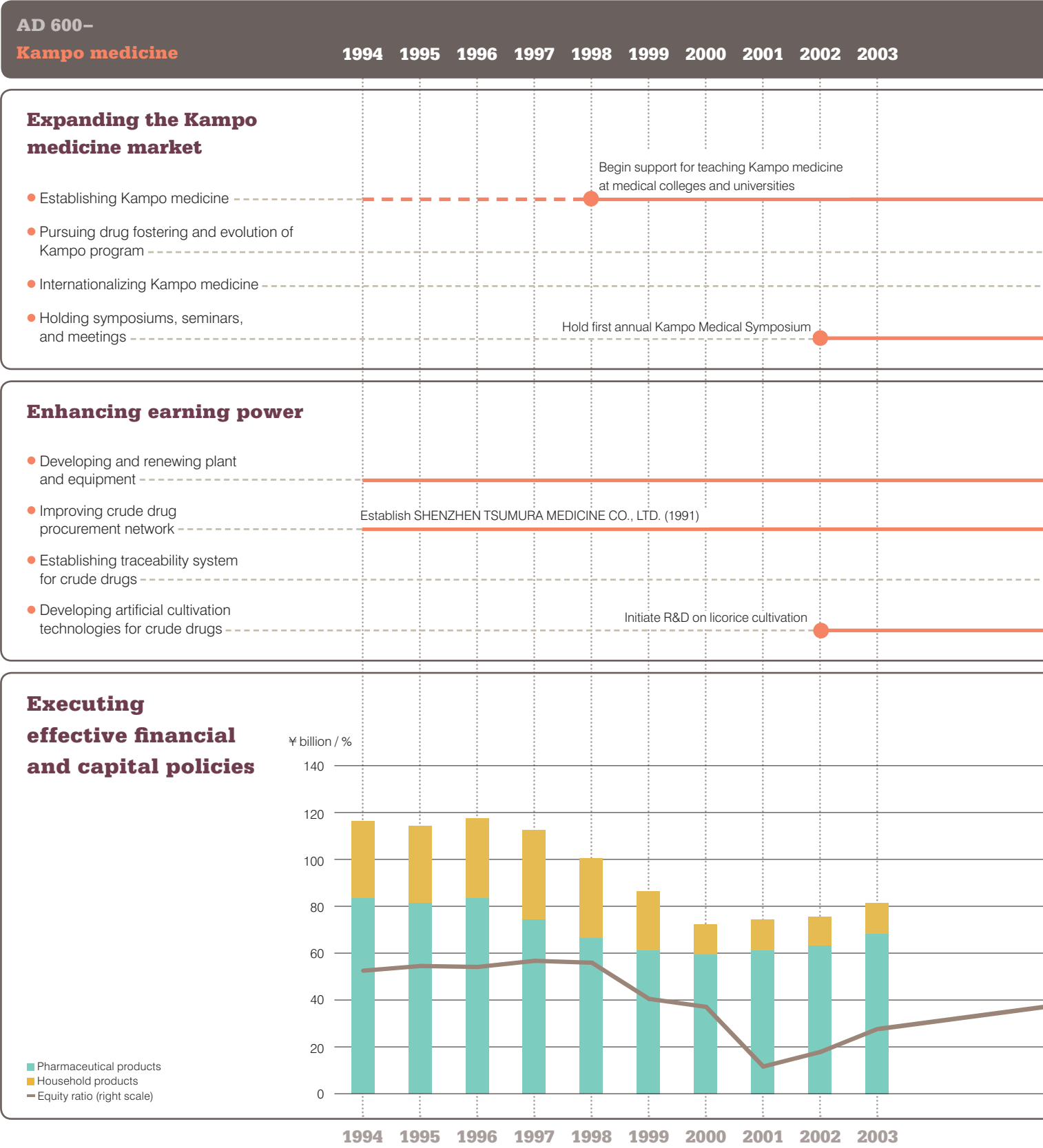
Tsumura's stable procurement of crude drugs depends on the farmers who cultivate crude drugs. In this article, a member of a Japanese producers' association talks about some interesting aspects of crude drug cultivation and the relationship of trust with Tsumura.

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Creating Long-Term Value: TSUMURA's Initiatives



2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 (FY)

Kampo medicine being taught at all medical colleges and universities

▶ P. 29

Start building body of scientific evidence for prescription Kampo products

▶ P. 28

Begin development of TU-100 (Daikenchuto) in the U.S.

▶ P. 30

Start Kampo seminars at designated hospitals for clinical training

▶ P. 21, 27

Establish YUBARI TSUMURA CO., LTD. /
LAO TSUMURA CO., LTD.

▶ P. 18, 19, 33

Start development of traceability system

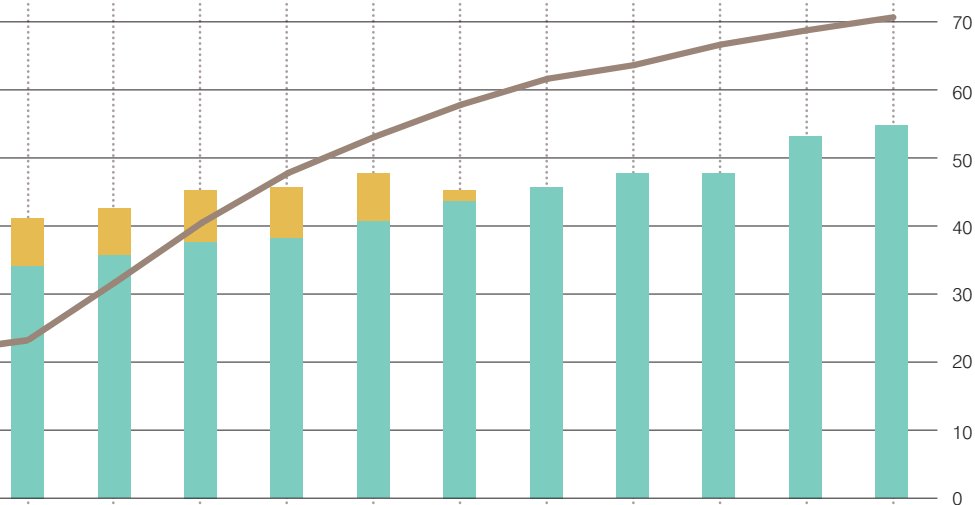
▶ P. 16, 17, 32,
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Complete development of licorice
cultivation technology

▶ P. 16, 17, 41

▶ P. 36

2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 (FY)

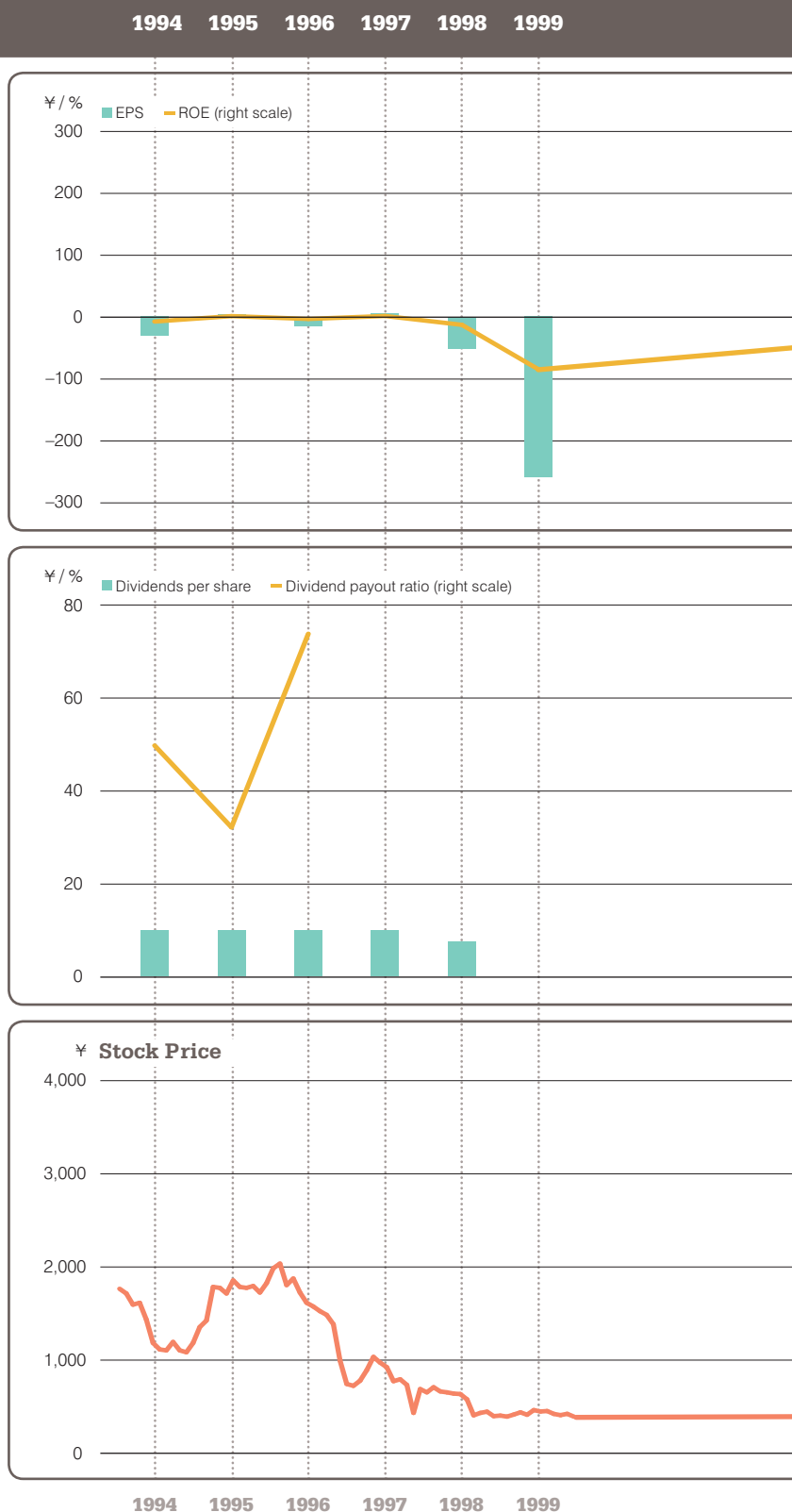


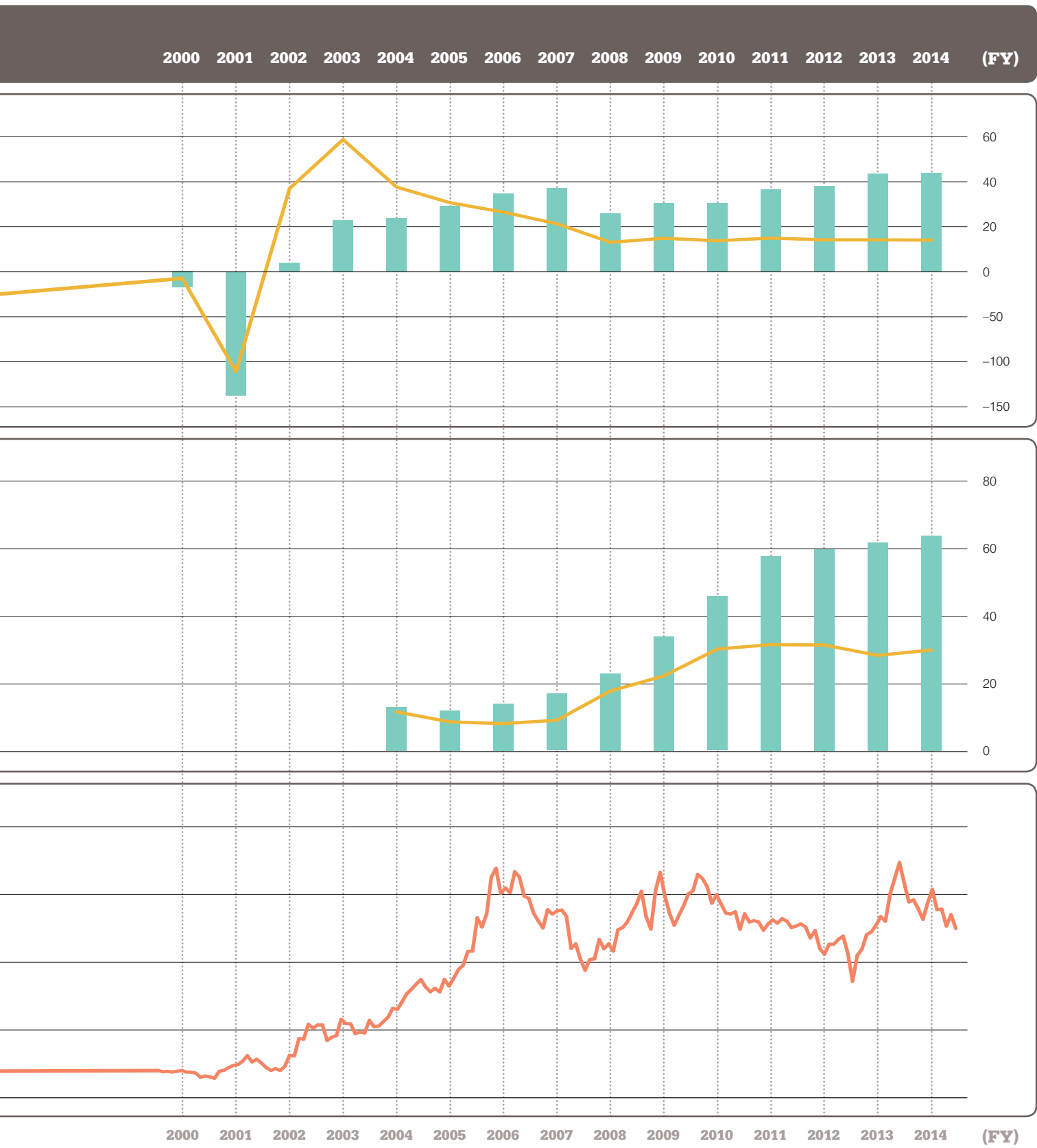
Creating Long-Term Value: TSUMURA's Track Record

Long-term value creation

Since its introduction into Japan in the sixth century, Kampo medicine has compiled a 1,400-year history as an accepted form of medicine, the raw materials of which are plants, minerals, and other elements derived from the cycle of nature. As a company operating a business based on a product with special features such as these, we have managed the business from a long-term perspective with the aim of future value creation. The strategic issues Tsumura is currently addressing in its medium-term management plan—"Expanding the Kampo medicine market," "Enhancing earning power," and "Executing effective financial and capital policies"—and our measures to attain the goals themselves are built on the efforts of the past. These goals are only possible because of our consistent work over the past 10 or even 20 years.

During the 1990s, Kampo product sales declined and businesses other than our core business at that time fell into the red. Tsumura went through a difficult period. Nevertheless, this experience enabled the Company to return to its roots and reaffirm its commitment to its Kampo medicine business. Thereafter, however, as a result of a steady drive to popularize Kampo medicine, our core business has continued to grow favorably since 2000 and achieved substantial improvements in efficiency. In particular, Tsumura has enjoyed the benefits of the results emerging from two programs over a long period that continues even today. One of them is the Kampo medicine education program that supports the teaching of Kampo medicine at medical colleges and universities in Japan with the goal of increasing the number of physicians who prescribe Kampo products in the future. The other program targets the establishment of a body of scientific evidence on the efficacy of Kampo medicine to build public trust in our products. Going forward, we will remain committed to pursuing measures and goals that will form the source of future growth in our corporate value.





Tsumura and Kampo

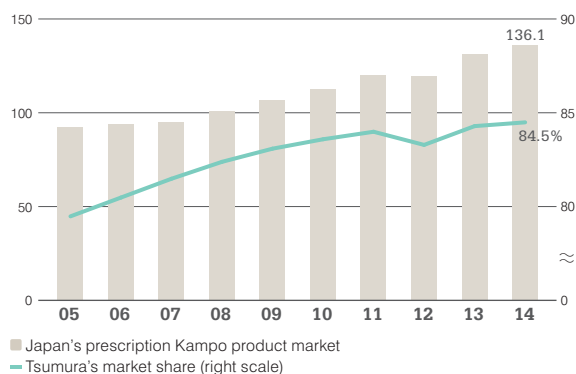
TRADITION COMBINED WITH ADVANCED TECHNOLOGY

Kampo medicine has been a traditional form of medicine in Japan for over 1,400 years. At the same time, however, our prescription Kampo products are also modern pharmaceuticals. The granulated formulations of the extracted active ingredients of crude drugs meet the strict specifications for coverage under the Japanese National Health Insurance (NHI) plan.



Size of Japan's Prescription Kampo Product Market and Tsumura's Market Share*

¥ billion / %



MARKET LEADER

Tsumura manufactures and sells 129 prescription Kampo products and accounts for a 84.5%* share of the market. As the market leader, it is also taking the lead in efforts to expand the domestic prescription Kampo product market.

* Copyright 2014 IMS Health. All rights reserved.
Estimated based on "IMS JPM Mar. 2005 MAT- Mar. 2014 MAT."
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RAW MATERIAL CRUDE DRUGS

Unlike Western drugs, which are manufactured from specific chemically synthesized substances, Kampo products are formulation mixtures of at least two and sometimes up to 10 different crude drugs. Consequently, a special characteristic of Kampo medicine is the inclusion of multiple active ingredients.





CRUDE DRUG CULTIVATION AND FARMING

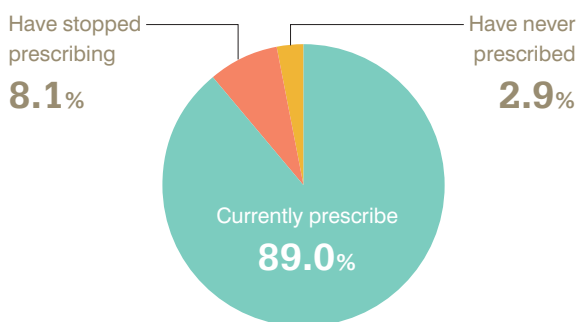
To secure a stable supply of the plants that make up the majority of the raw material crude drugs, Tsumura cultivates crude drugs on its Cultivated Land under Own Management* in Japan and Laos. The Company supplements those sources through a network of farmers and agricultural organizations built up over the years.

* Farms with a certain scale of cultivation area for which Tsumura directly provides cultivation guidance and has an understanding of cultivation costs and can set procurement prices.

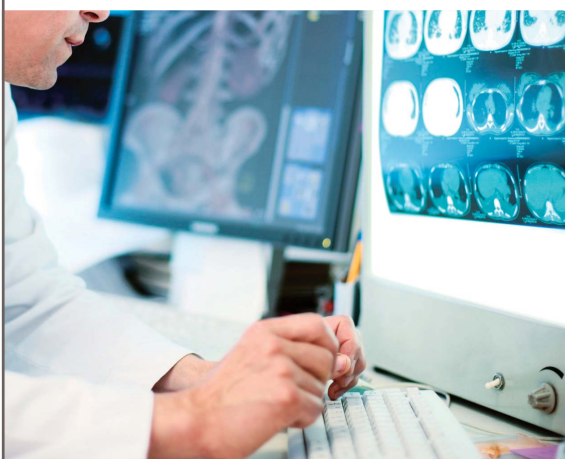
EXPANDING PRESCRIPTIONS BY PHYSICIANS

In Japan, there is only one class of medical license—each individual physician can prescribe both Kampo products and Western drugs for patients. Given these circumstances, physicians are increasingly prescribing Kampo products because of the mounting body of scientific evidence on its efficacy. These days, close to 90% of Japan's physicians have prescribed Kampo products for their patients.

Kampo Medicine Disbursements by Physicians (Valid number of responses=627)



Source: 2011 Survey on Prescribing Kampo Products, the Japan Kampo Medicines Manufacturers Association



EXTENDING THE SCOPE OF PRESCRIPTIONS

Traditionally, Kampo products have primarily been prescribed for patients with internal complaints. Today, however, the scope of medical conditions for which they are prescribed has expanded to span the fields of mental and geriatric disorders to surgery. In recent years, Kampo products are also being used in oncology and other advanced medical treatment areas.

Financial Highlights

TSUMURA & CO. and subsidiaries
Years ended March 31

Sales

+4.2%

YoY

ROE

+0.4 pt

YoY

Dividend

+¥2

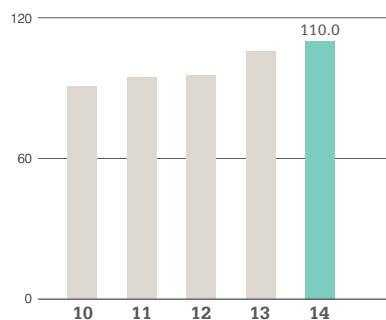
YoY

	2010	2011	2012	2013	¥ in millions 2014	US\$ in thousands* 2014
For the year						
Net sales	¥90,933	¥94,778	¥95,450	¥105,638	¥110,057	\$1,069,352
Sales of prescription Kampo products	83,782	89,247	89,964	99,457	102,680	
Operating income	18,938	21,553	21,233	23,124	22,461	218,243
Net income	10,704	12,945	13,431	15,373	18,050	175,385
Selling, general and administrative expenses	43,475	43,789	44,271	46,586	48,808	474,235
R&D expenses	3,770	4,123	4,565	4,904	5,949	57,807
Depreciation	3,225	3,453	3,850	4,049	4,871	47,328
Capital expenditures for property, plant and equipment	5,237	5,264	6,425	9,328	8,991	
At year-end						
Total assets	¥134,697	¥141,549	¥151,874	¥170,466	¥187,623	\$1,823,006
Total net assets	83,752	91,154	102,240	118,537	133,318	1,295,357
Interest-bearing debt	23,204	23,086	22,070	22,059	22,088	214,616
Other selected data						
Cash flows from operating activities	¥12,019	¥12,047	¥7,314	¥12,011	¥5,908	\$57,412
Cash flows from investing activities	(6,155)	(6,815)	(5,342)	(8,022)	(1,694)	(16,464)
Cash flows from financing activities	(5,085)	(3,355)	(5,272)	(4,275)	(4,575)	(44,454)
Per share data (yen/dollars)						
Net income	¥ 151.77	¥ 183.55	¥ 190.45	¥ 217.98	¥ 255.94	\$ 2.48
Dividends	46.00	58.00	60.00	62.00	64.00	
Net assets	1,175.04	1,274.06	1,430.94	1,658.88	1,860.14	18.07
Financial ratios (%)						
Operating income margin	20.8	22.7	22.2	21.9	20.4	
ROE	13.7	15.0	14.1	14.1	14.5	
ROA	14.5	15.6	14.5	14.3	12.5	

* U.S. dollar amounts have been translated from yen, for convenience only, at the rate of ¥102.92=U.S.\$1, the prevailing Tokyo foreign exchange market rate as of March 31, 2014.

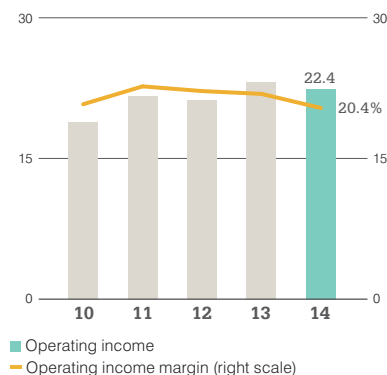
Net Sales

¥ billion



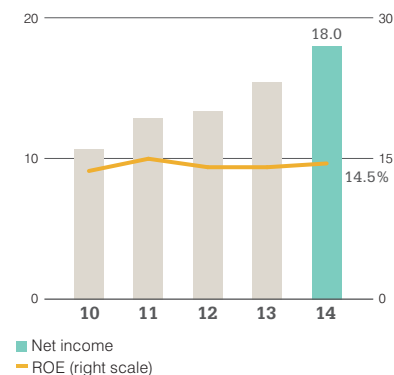
Operating Income / Operating Income Margin

¥ billion / %



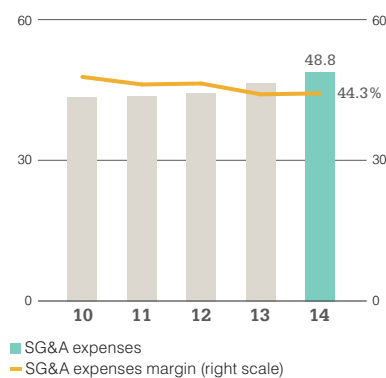
Net Income / ROE

¥ billion / %



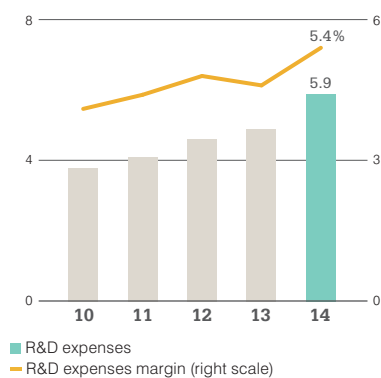
SG&A Expenses / SG&A Expenses Margin

¥ billion / %



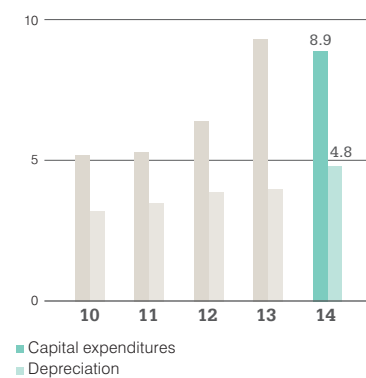
R&D Expenses / R&D Expenses Margin

¥ billion / %



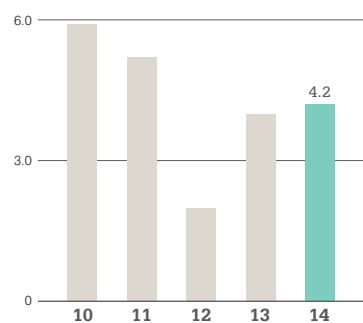
Capital Expenditures / Depreciation

¥ billion



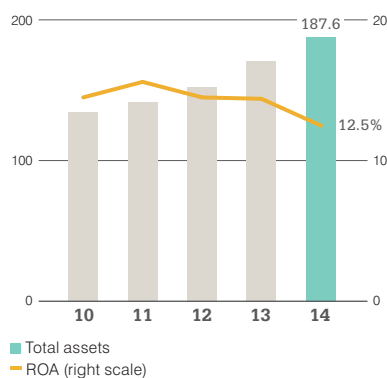
Free Cash Flow

¥ billion



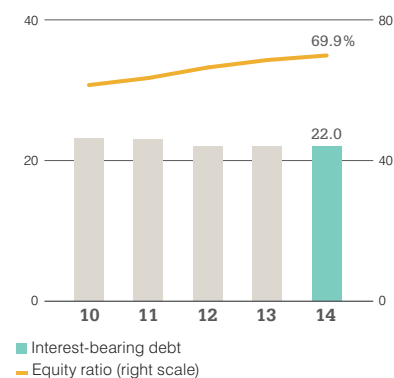
Total Assets / ROA

¥ billion / %



Interest-Bearing Debt / Equity Ratio

¥ billion / %



To Our Stakeholders

Our efforts to strengthen our operating base, with a view to Tsumura 10 years from now, are proceeding favorably. The Company is working to implement strategies and attain sustainable growth to achieve its long-term vision.

Fiscal 2014, the fiscal year ended March 2014, was the second year of our first stage medium-term management plan targeting the realization of the goals of our long-term business vision—"Aim to be a value-creation company that contributes to people's health through its Kampo medicine business." Let me begin by reporting to our stakeholders that it was a year in which we made steady progress with measures regarding our strategic issues set out in our medium-term management plan based on its theme, "Strengthening the growth base."

Our Company's strategic issues, namely expanding the Kampo medicine market, enhancing earning power, and increasing corporate value by executing effective financial and capital policies, are not tasks that you begin today and complete tomorrow. Furthermore, we cannot expect to see immediate results, and in some cases it may take several years for results to emerge. However, Tsumura's performance over the last 20 years shows that these continued efforts regarding our strategic issues have contributed to medium- to long-term growth.

It is of course important for the Company to fulfill the expectations of its stakeholders on an annual basis. Nevertheless, I believe that a much bigger mission for myself as CEO is to plan for Tsumura's growth 10 years from now and to achieve enhanced corporate value in the medium to long term. In the following sections, I will report on the actions we are taking currently, our outlook for the future, and our goals based on a business vision targeting the achievement of growth in corporate value from a long-term perspective.



Fiscal 2014 Business Results and Performance Forecasts for Fiscal 2015

In fiscal 2014, consolidated net sales increased 4.2%, to ¥110,057 million, while operating income declined 2.9%, to ¥22,461 million. Although overall sales of our 129 prescription Kampo products grew 3.2% year on year, operating income declined primarily because of rising prices for raw material crude drugs.

Looking at net income, as a result of the booking of extraordinary gain on the sale of investment securities and other factors, net income rose 17.4%, to ¥18,050 million. Not only did we remain true to our policy of emphasizing stable dividend payments, we increased the year-end dividend by ¥2 per share, resulting in annual dividends of ¥64 per share.

In fiscal 2015, we expect demand for our prescription Kampo products to reflect the steady expansion in the market

by continuing to grow. However, taking into consideration the official drug price revision in April 2014, we expect net sales growth will be held to 1.2%. Taking into account that operating income will be similarly affected by the official drug price revision, increases in the prices of some raw material crude drugs, exchange rate impacts, and other factors, we are estimating that operating income will decline 19.0%.

Fiscal 2015 Performance Forecast

¥ million / %	
Net sales	111,400
Operating income	18,200
Net income	11,800
Operating income margin	16.3%

Note: The performance forecast above is established based on the information available as of May 12, 2014 and is also subject to certain assumptions. Therefore, our actual financial performance may differ.

Fiscal 2014 Business Results

¥ million

	Plan	FY2014	Vs. Planned		YoY	
			Amount	Difference	Amount	Change
Net sales	109,000	110,057	1,057	1.0%	4,418	4.2%
Operating income	22,000	22,461	461	2.1%	-663	-2.9%
Net income	17,700	18,050	350	2.0%	2,677	17.4%
Operating income margin	20.2%	20.4%		+0.2 pts		-1.5 pts

Medium- to Long-Term Market Outlook

Japan is one of the countries with the most-aged populations in the world. At January 1, 2014, people aged 65 years or older accounted for 25.2% of Japan's total population of 127.2 million.*¹ Because of the declining proportion of young people caused by low birth rates, this figure is expected to rise to 29.1% by 2020.*² Considering these changes in Japan's demographics, we see three potential benefits for Tsumura's operations.

The first potential benefit is the growth in demand related to medical treatment of the elderly. Among the elderly, the proportion of patients with multiple chronic diseases is increasing. If these multiple chronic diseases were only to be treated with Western medicine, it would place a heavy burden on the elderly patients who would have to visit multiple specialty medical departments and manage a large volume and increased number of medications. On the other hand, the basic principle of Kampo medicine is to treat the patient

To Our Stakeholders

based on an assessment of their overall condition. In addition, using the special characteristic of Kampo medicine—multiple ingredients—it is possible to treat a patient for multiple diseases with one formulation. For those reasons, it can be said that Kampo medicine is a treatment method that places relatively little burden on the elderly, who need to have their illnesses treated on a long-term basis.

The second potential benefit is the expanded need for primary care. In view of the increase in the number of elderly due to the aging population and the related increase in healthcare costs, a debate has begun in Japan on the value of the current general physician system as a medical specialist. Moreover, in the National Health Insurance (NHI) plan's April 2014 review of medical treatment compensation, a regional comprehensive care fee system and other measures were set up that positively evaluates family physicians (primary care physicians) who handle all of a patient's overall healthcare needs on an ongoing basis. In fact, there is a movement under way to expand such comprehensive medical treatment systems on a regional basis. In this changing climate, we have expectations that these trends will lead to expanded use of Kampo medicine, which is based on considering a patient's overall condition.

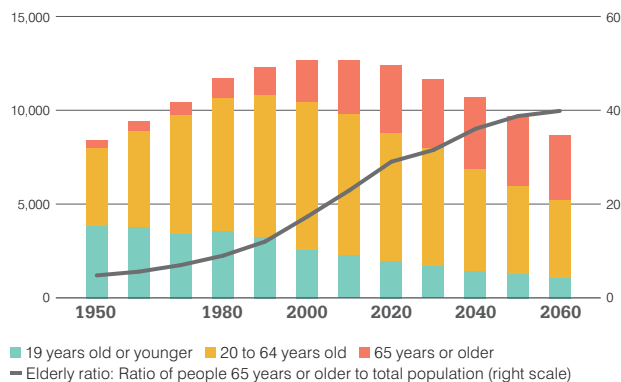
The final potential benefit is the increased number of women joining the workforce. Against the backdrop of a shrinking labor force caused by low birth rates and the aging population, we can expect the number of women with jobs to continue to grow. Kampo medicine is already well known for being effective in treating gynecological disorders. However, in recent years, working women have also taken an interest in Kampo medicine because its effects, such as adverse reactions, are relatively mild and put less strain on the body. For this reason, demand for Kampo medicine by working women is expected to increase.

¹ Statistics Bureau, Ministry of Internal Affairs and Communications, "Population Estimates" (January 2014 (Final estimates) June 2014 (Provisional estimates)) (Announced June 20, 2014)
<http://www.stat.go.jp/data/jinsui/new.htm>

² Cabinet Office, "Fiscal 2013 White Paper on Aging Society"

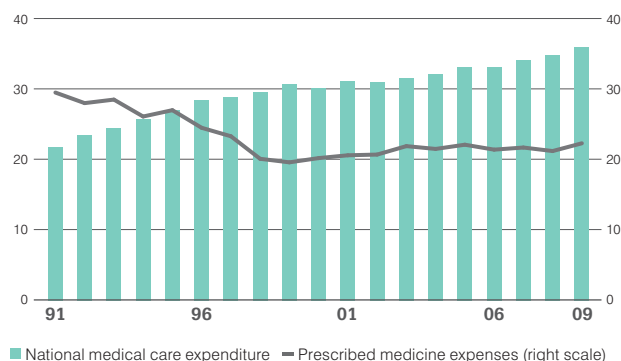
Japan's Population Forecast and Aging Demographic

Ten thousand people / %



Trends in National Medical Care Expenditure and Prescribed Medicine Expenses

¥ trillion / %



Expanding the Kampo Medicine Market

Anticipating these long-term shifts in the market, we are proceeding with our efforts to strengthen the growth base to achieve greater value creation. To that end, we are pursuing the three strategic issues of expanding the Kampo medicine market, enhancing earning power, and increasing corporate value by executing effective financial and capital policies.

To expand the Kampo market, we are especially strengthening our marketing approach to designated hospitals for clinical training. Specifically, our medical representatives (MRs) are

holding Kampo study groups to explain the efficacy and benefits of Kampo products for physicians-in-training at designated hospitals for clinical training and university hospitals. The MRs also hold Kampo medicine and product information meetings for practicing physicians. Our goal is to systematically increase the number of physicians with an interest in using Kampo products in the clinical workplace. Our MRs are achieving this goal by targeting physicians who have received an education in Kampo medicine at medical colleges and universities, passed the medical examination, and are working as physicians-in-training as well as all medical specialty departments at designated hospitals for clinical training and university hospitals.

We are making steady progress with establishing a body of scientific evidence for our first “drug fostering” program formulations. The same can be said for our efforts to develop TU-100 (Daikenchuto) in the United States. Both of these measures are not going to show immediate results. However, by steadily moving forward while keeping an eye on how effective the programs are, these measures will contribute to the medium- to long-term expansion of the Kampo market—and hence the growth of Tsumura.

Enhancing Earning Power

As shown by the impact of higher crude drug prices on fiscal 2014 profit performance, the securing of raw material crude drugs and the stabilization of their prices are important issues for the Company. Toward a resolution of these issues, for the past two years, Tsumura has been taking steps to expand its Cultivated Land under Own Management.*³ In addition to farmland directly managed by the Company or its subsidiaries, Cultivated Land under Own Management includes the farmland owned by Japanese and Chinese production companies under contract to Tsumura. Through this system, we are focusing on establishing a scheme whereby the Company can procure the raw material crude drugs it needs at prices relatively unaffected by market price fluctuations. Measures being implemented include improving production efficiency and increasing crop yields per unit of area.

We are also working on reforming the cost structure by improving labor productivity. Under our medium-term management plan, Tsumura has invested record levels of approximately ¥9 billion in capital investments in both fiscal 2013 and fiscal 2014 to expand the production capacities of existing plants and introduce the most-advanced manufacturing technologies. Action plans to reduce our labor force and energy consumption have already been completed. Therefore, when production volumes rise in the future, we expect to see a proportional decline in our unit manufacturing costs.

*3 Farms with a certain scale of cultivation area for which Tsumura directly provides cultivation guidance and has an understanding of cultivation costs and can set procurement prices.

Strategic Issues Under the Medium-Term Management Plan

Expanding the Kampo Medicine Market

Expand the prescription
Kampo product market in Japan

Enhancing Earning Power

Reform the Company's cost
structure through the introduction
of new technology and
other measures

Executing Effective Financial and Capital Policies

Increase corporate value
by executing effective financial
and capital policies

To Our Stakeholders

Executing Effective Financial and Capital Policies

While we try to maintain a balance between our capital investments for future growth and returning profits to shareholders, I believe there is an even higher priority policy the Company must follow to fulfill our shareholders' and other investors' expectations of Tsumura. That policy is to endeavor to increase our corporate value through the continuous growth of our Kampo product and crude drug operations. Currently, we are considering raising funds to allocate to capital investments for growth. We plan to make that decision, however, based on careful consideration of the cost of capital and the financing method.

There are no other listed companies in Japan that have prescription Kampo product manufacturing and sales as their core business. In fact, Tsumura has established a unique position for itself not only in Japan's industry, but also in the global pharmaceutical industry. To convert that uniqueness and our contribution to medical treatment into growth in corporate value, we are pursuing the goals of our strategic issues.

Tsumura's Business Resources: A Growth Base Founded on Trust

I believe that our crude drug procurement network ranks equally with our human resources as our most important business resource. In ensuring the quality of our prescription Kampo products, the quality of our crude drugs is the deciding factor. For that reason, a network of producers who understand our preoccupation with quality and with whom we have a mutually sympathetic and trusting relationship has irreplaceable value for our Company.

Over the past year, I travelled to China frequently and had the opportunity to discuss our business with representatives of production companies. When the market price of a crude drug rises, it is not surprising that some of these production companies would want to sell their crops to buyers other than Tsumura. Therefore, it was heartening to hear from one of those representatives that "Once I did ship our product to somebody else, but after thinking about it realized that from a long-term point of view, clearly the Tsumura contract was the better deal, so I came back." I am proud that while our policy of trying to stabilize our procurement of crude drugs by building trustworthy long-term relationships may seem roundabout, it is in fact the best way to build a solid foundation for the future.

Going forward, I intend to continue to work to fulfill the expectations of patients, the healthcare community, shareholders and other investors, and other stakeholders. I am determined to do so by taking action—sometimes cautiously, sometimes boldly—that will contribute to growth in Tsumura's corporate value.

August 2014



Terukazu Kato
President, Representative Director



Tsumura's Commitment to Long-Term Value Creation

Tsumura has built a proprietary Kampo value chain to enable the stable production and supply of a total of 129 high-quality prescription Kampo products. And we are constantly working to enhance that value chain. In the following section, we look at Tsumura's long-term-oriented value-creation activities and the business resources the Company has accumulated along the way.

Kampo Value Chain



Establishing a Producers' Network



Establishing a producers' network supports the procurement of high-quality raw material crude drugs and the sustainable growth of Tsumura.

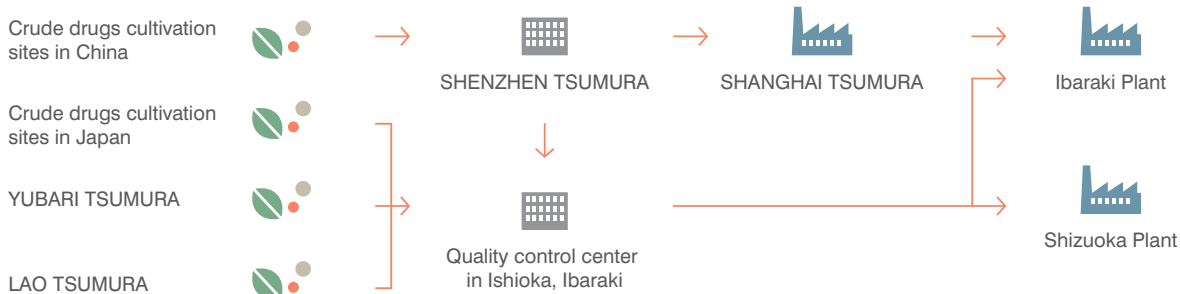
The stable production and procurement of crude drugs, the raw materials for Kampo products, underpin Tsumura's Kampo medicine operations. Among the important raw material crude drugs for our operations, there are some raw material crude drugs that require an environment not available in Japan. Therefore, the securing of a supply of consistent high-quality raw material crude drugs in sufficient volumes from China is a critical management issue for developing business operations and for achieving future business growth.

Because the Company sources approximately 80% of its raw material crude drugs in China, SHENZHEN TSUMURA MEDICINE CO., LTD., has an important role to play in the process. The Chinese subsidiary's role is not limited to providing the procurement, processing, quality inspection, and storage functions. It also acts as the traceability base for raw material crude drugs produced in China by collecting information on production regions and providing guidance and other support to local producers.

There is a profusion of local production companies and related companies that organize farmers involved with the cultivation and processing of crude drugs in China. From among them, Tsumura has sought out those production companies that understand their support role in supplying raw materials for safe Kampo products that patients can be confident in using and that take pride in their work.

Procurement of a stable supply of high-quality raw material crude drugs requires the establishment of a network based on good relationships with producers. We are strengthening the collaborative relationship with producers and local production companies that sympathize with our policy of achieving stable supplies and maintaining a strict quality standard. Furthermore, we are pursuing the expansion of Cultivated Land under Own Management principally through local production companies with a view to mitigating crude drug price movements and setting the stage for future business expansion.

Sharing Traceability Information



Liu Yude

Chairman of the Board
SHENZHEN TSUMURA MEDICINE CO., LTD.



When looking at a new production company to add to the network, SHENZHEN TSUMURA MEDICINE always invites them on a tour of the subsidiary or a model local production company to give them an opportunity to gain an understanding of our policies and Tsumura's GACP.* Producers may say that we are very demanding when it comes to the quality of raw material crude drugs, but we also have a reputation of being a company that can be trusted and does business on a long-term basis.

What we are most proud of is the widely held opinion that "Doing crude drug business with SHENZHEN TSUMURA MEDICINE is a learning experience for both farmers and production companies." In addition to procuring crude drugs from farmers, our collaborative local production companies play an important role in providing cultivation guidance, instruction on the efficient use of cultivation machinery and equipment, and other support. They are passing on knowledge, technologies, and know-how that only Tsumura can provide. We also are emphasizing placing our own staff in the production companies of our network to provide instruction in processing or training in crude drug quality management.

Collaboration with production companies is also essential in expanding Cultivated Land under Own Management. It is not easy to assess a production company's capability for managing Cultivated Land under Own Management keeping in mind the varieties of crude drugs that are top priority for Tsumura and for which cultivation technology is relatively well established. However, it also represents a chance to deepen our relationship with the production company. Therefore, I believe that this process represents an important investment in our future growth.

Since its establishment in 1991, SHENZHEN TSUMURA MEDICINE has been in operation for 23 years. During that time, we have become recognized by Chinese government organizations and the pharmaceutical industry as a model company for the production and procurement of crude drugs. In future, we will endeavor to procure raw material crude drugs that have been meticulously checked for quality based on our network of production companies. Our aim is to be the control tower for the supplies of raw material crude drugs from China.

* Good Agricultural and Collection Practices



Licorice cultivation field



SHENZHEN TSUMURA MEDICINE CO., LTD.

Accumulating Manufacturing Technology and Know-How



Demonstrating the know-how and technological capabilities required to manufacture its 129 Kampo formulations, Tsumura is implementing manufacturing innovations for further growth.

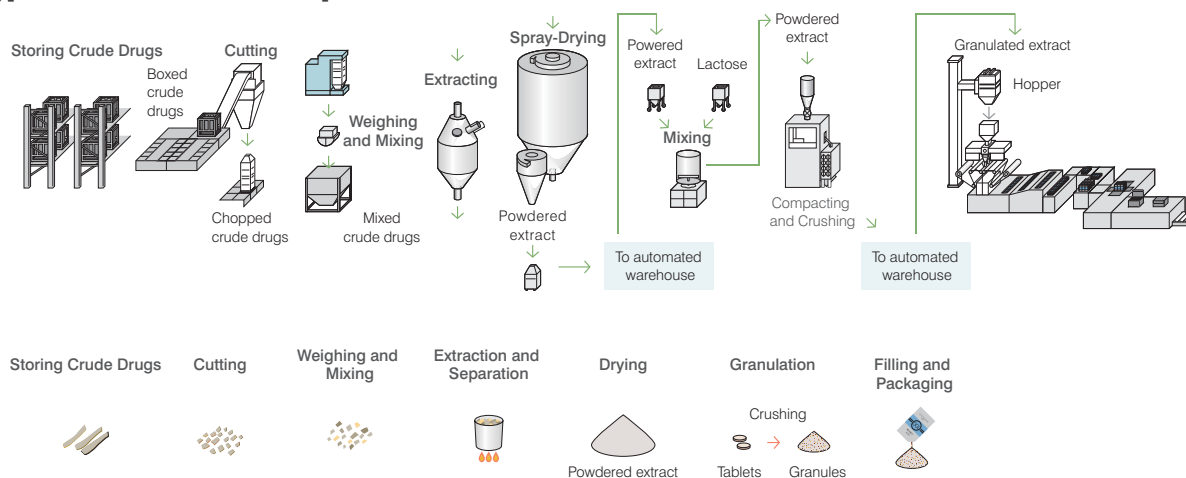
One of the characteristics of Kampo product manufacturing facilities is the large variety of raw materials used, which come in a variety of forms. In manufacturing its 129 Kampo products, Tsumura requires close to 120 different raw materials just in terms of species. Moreover, even though the raw materials are dried, some, such as the roots of trees or bark, are hard, some, such as leaves, are soft and light, and some, such as minerals, are heavy. One of the requirements of Kampo formulation manufacturing facilities and processes is a design that accommodates the nature of the different raw materials.

In addition, to produce 129 different Kampo formulations, the manufacturing facilities must be able to handle multi-product production. Since the production runs may be

limited to small lots depending on the formulation, the manufacturing line must be easy and quick to retool and thoroughly cleaned between runs to ensure no contamination by other formulations. While Tsumura's facilities must comply of course with Japan's GMP standards, the facilities are now going to also have to comply with the global standards of PIC/S GMP.*

Because the crude drugs come from living organisms, there will be a certain degree of variance in their ingredient amounts and other factors. Being able to consistently manufacture high-quality Kampo products without any variance in ingredients between production lots requires the accumulation of a great deal of advanced know-how and technology.

Typical Production Flow for Kampo Products



* Good Manufacturing Practices are manufacturing standards set by the Minister of Health, Labour and Welfare as stipulated in the Pharmaceutical Affairs Act. Since Japan became a participant in the Pharmaceutical Inspection Convention and Pharmaceutical Inspection Co-operation Scheme (PIC/S) in July 2014, various changes are expected in these standards.



Kimitoshi Usui

Corporate Officer
Head of Production Division

Tsumura built its manufacturing facilities according to its own design. The facilities themselves contain almost no general-use equipment, almost all of the equipment with the previously mentioned characteristic of using a large variety of raw materials is custom made. Both the Shizuoka Plant, which began operations in 1964, and the Ibaraki Plant, which came on stream in 1983, were constructed over the course of many discussions with an engineering company that Tsumura has had developed a partnership with over the years. As a result, each of the pieces of equipment incorporate the accumulated knowledge and technology of the Company.

Currently, Tsumura is proceeding with measures to increase the production capacity of its existing manufacturing facilities and to improve its cost structure through the introduction of new manufacturing technologies. The primary means of increasing the production capacity of the existing manufacturing facilities will be achieving continuous around-the-clock manufacturing. The Company is developing an automated monitoring system that quantitatively monitors

operating conditions to enable safe operations even when operators are not directly operating the manufacturing lines. The focus of the new manufacturing technology being introduced is manpower and labor savings. Already, the conveyor process that moves large volumes of raw material crude drugs to and from the warehouses and into the plant is almost fully automated. In addition, robots have been installed to rotate or move heavy objects.

The issue being directly faced by the Production Division is accomplishing the successful introduction of new manufacturing technology in our manufacturing facilities. Under Tsumura's medium-term management plan, we are aiming to increase labor productivity by about 30% by fiscal 2017 compared with fiscal 2012. Based on that plan, we intend to fully employ the performance capability of the new manufacturing facilities that are in operation to improve productivity and to expand production capacity to set the stage for future growth.



Weighing and mixing



Spray dryer



Robot-based palletizer transport

Developing Communication Channels with Physicians



Our medical representatives (MRs) do not simply sell our products, they work in partnership with physicians that have an interest in Kampo medicine, serving the role of expanding the physician’s knowledge and understanding of this field.

To expand the Kampo market, Tsumura has implemented its establishment of Kampo medicine programs, in other words, its activities to enhance, establish, and develop Kampo medicine. When we began our support for Kampo medicine education, there were many physicians who really did not understand Kampo medicine. However, in March 2001, the Ministry of Education, Culture, Sports, Science and Technology announced the inclusion of the requirement of “a general understanding of Japanese Kampo” for graduating medical students in the “medical education model core curriculum.” Thanks to that requirement, there has been a sharp increase in understanding of and interest in Kampo medicine among physicians over the following years.

Taking advantage of this heightened interest in Kampo medicine, in recent years Tsumura has strengthened its

marketing approach to designated hospitals for clinical training by providing Kampo medicine education support for physicians that have just graduated in addition to conducting its usual support programs for medical colleges and universities. Specifically, we have held Kampo study groups for physicians-in-training at 1,000 designated hospitals for clinical training nationwide. Moreover, making use of our extensive product line of 129 Kampo formulations and their wide range of efficacies and benefits, we conducted Kampo medicine and product information meetings targeting the approximately 18,000 medical specialty departments at designated hospitals for clinical training. During fiscal 2014, we held Kampo medicine and product information meetings at 12,845 medical specialty departments, approximately 71% of the targeted group.

Information Support for Physicians	
Tsumura's approach	Details
Sales visits and meetings	Visit physicians individually, supplying them with information according to their needs. If they are showing an interest in Kampo medicine for the first time, explain formulations that have the highest success rates.
Medical department information meetings	Explain the body of scientific evidence on Kampo medicine gathered by the "drug fostering" program and the current status of Kampo medicine treatments to individual groups of research and diagnostic physicians in specialty departments at university hospitals and hospitals.
Kampo medicine seminars (Introductory seminars)	Seminars are held all-year-round targeting physicians already working in the clinical field, but have never had the opportunity to study Kampo medicine.
Kampo medicine seminars (Step-up seminars)	These seminars target physicians that have previously taken the introductory course and provide other physicians with an opportunity to increase their knowledge of Kampo medicine and products.
Kampo medicine seminars for designated hospitals for clinical training	In this category, Tsumura targets providing information on Kampo medicine to physicians and lecturers in Kampo medicine at medical colleges and universities. In addition, Tsumura holds its Kampo Medical Symposium annually, bringing education-related people together under one roof to discuss Kampo medicine education issues and best practices.
Kampo medicine seminars for Kampo medicine lecturers Kampo Medical Symposium	



Ryouichi Murata

Corporate Officer
Head of Sales & Marketing Division

One of the characteristics of Tsumura's MR activities is our focus on providing information on Kampo medicine along with information on our Kampo products. In general, it can be said that there still are not many physicians in regular medical departments that have a high degree of understanding of Kampo medicine. As a result, our MRs do not only explain the efficacies and benefits of each of our formulations, they promote understanding of Kampo medicine in terms of improving the healing process of patients for whom treatment with Western medicine has limits and suggest a combined treatment method.

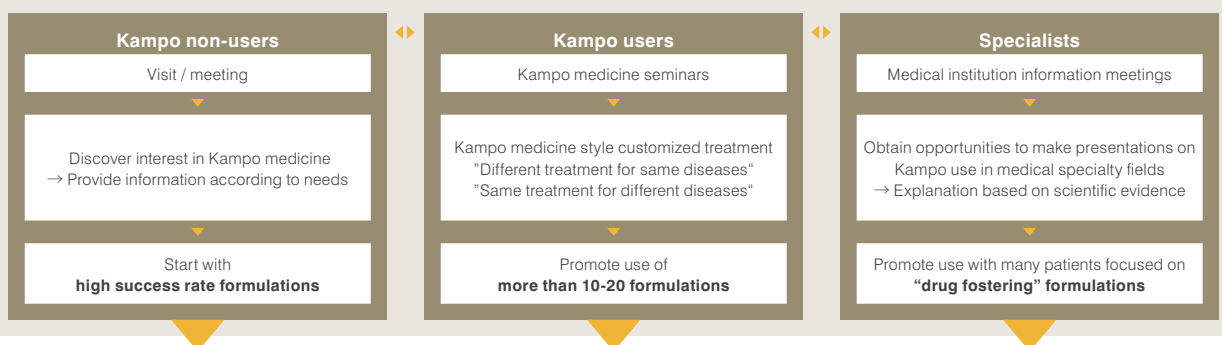
In establishing a common ground with physicians, Tsumura's program to establish a body of scientific evidence on the efficacy of Kampo products has great significance. Now that work on the body of scientific evidence has progressed, the fact that many clinical physicians that try prescribing Kampo formulations for their patients go on to prescribe many more types of Kampo formulations suggests that the medicine is effective.

We frequently hear about physicians saying how disorders that they had unsuccessfully tried to treat with different Western drugs improved when treated with Kampo products. Our MRs also report that in such cases many of the physicians become motivated to take an interest in or learn about Kampo medicine after their patients express their gratitude for the improvement in their condition. If our MRs effectively approach these physicians with an interest in studying Kampo medicine, it results in an active transfer and exchange of information between the MRs and physicians about Kampo medicine and Kampo products.

As interest in Kampo medicine continues to spread further among physicians, we believe that the number of physicians prescribing 10 or 20 formulations will increase. We need to raise the ability level of our MRs to meet growing information needs of physicians.

Expansion Strategy for Kampo Medicine Market

Physicians at clinics, hospitals, designated hospitals for clinical training, university hospitals, and in all medical specialties



Kampo products used in daily medical practice in all medical institutions and specialty fields

Kampo Value Chain



Enhancing Corporate Value Through Long-Term Measures to Build Business Resources That Are Reinvested in the Kampo Value Chain.

The stages of the Kampo value chain cover an extremely wide range of activities. Producing, procuring, and managing the quality of crude drugs, the raw materials for prescription Kampo products, managing crude drug storage facilities to ensure a stable supply, manufacturing and granulating high-quality powdered extract, and running programs to popularize the use of Kampo medicine are all part of the Kampo value chain. In addition to the broad scope of activities, the extended timeframe of many of those activities is characteristic of the Kampo value chain. We procure crude drugs from farmers based on a cultivation contract that, depending on the variety of crude drug, can take around five years to harvest. Another example of the long-term nature of our activities is our program to continuously support Kampo medicine education for physicians before and directly after their graduation and on an ongoing basis. The activities of the Kampo value chain are also spread over a wide area geographically. In addition to our Japanese operations, we procure approximately 80% of our crude drugs from China, another 5% from Laos, and also manufacture powdered extract at our factory in China. As can be seen, the building of a Kampo value chain covering such a broad range of activities, timeframes, and geographical areas does not happen overnight—it requires a long-term commitment to its management and enhancement.

The end result of our long-term, continuous measures to establish a producers' network, accumulate manufacturing technologies and know-how, and develop communication channels with physicians is the creation of business resources that have significant value for our business. The input of these business resources enhances our Kampo value chain and contributes to placing Tsumura in a market position unassailable by competitors.

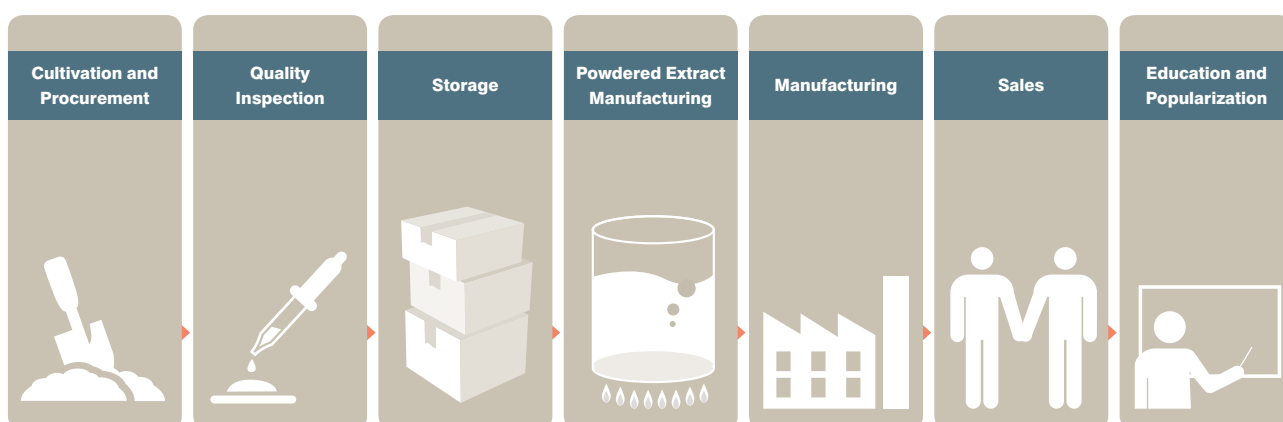
The cornerstone of these business assets is our human resources. As a company in the extremely unique business of manufacturing and selling Kampo products, we are continually working on the frontier, whether it is the procurement of raw materials, developing manufacturing technology, or communicating with our stakeholders. People who can generate their own solutions and find a path forward are a prerequisite for maintaining and building our business resources.

As Tsumura continues to move forward, we will aim to achieve business growth and continuous value creation by establishing an energetic organization founded on a stable financial base and by building our business resources from a long-term point of view.

Increasing corporate value over the long term

Achieving the goals of the Medium-Term Management Plan

KAMPO VALUE CHAIN



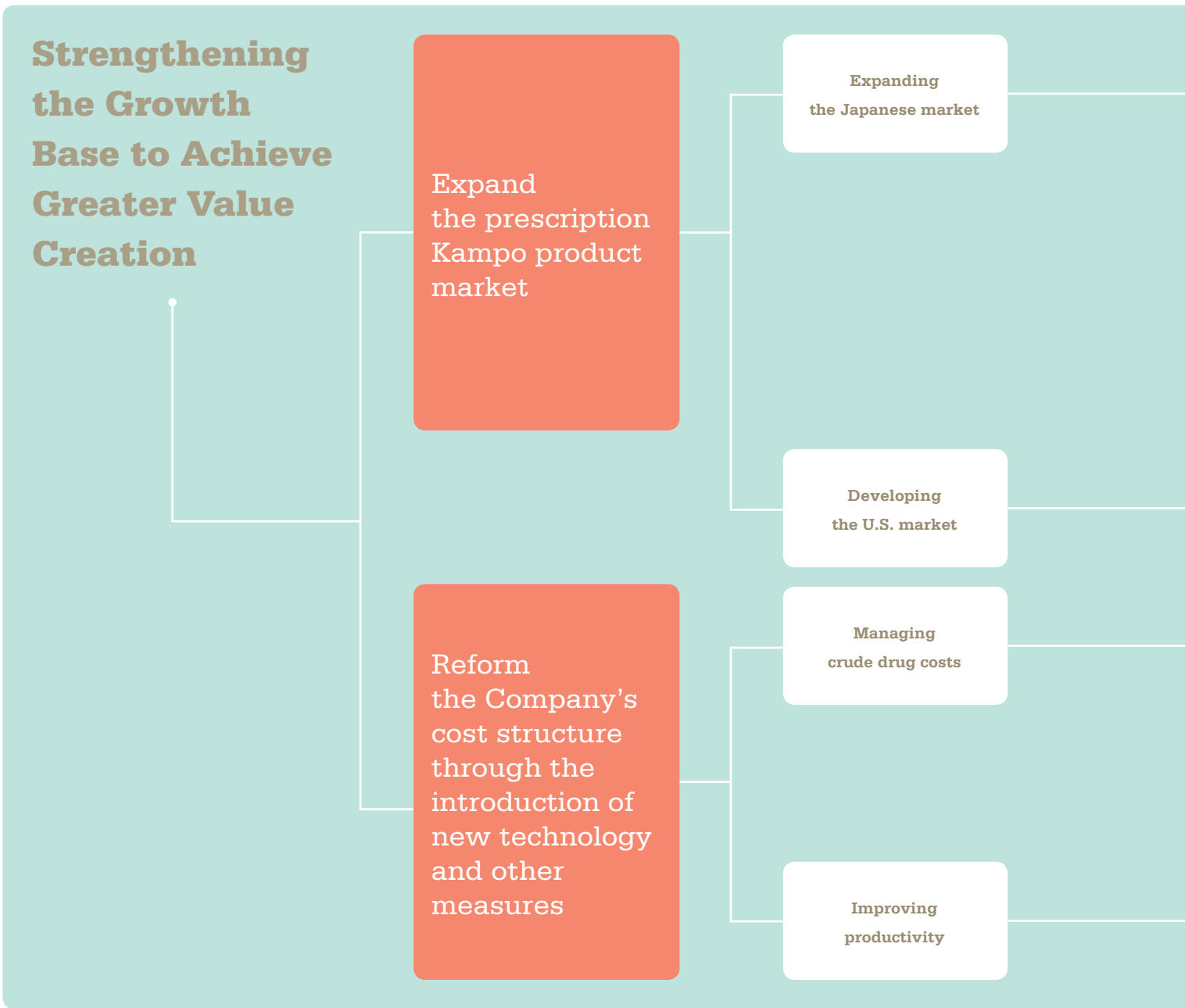
MANAGEMENT CAPITAL



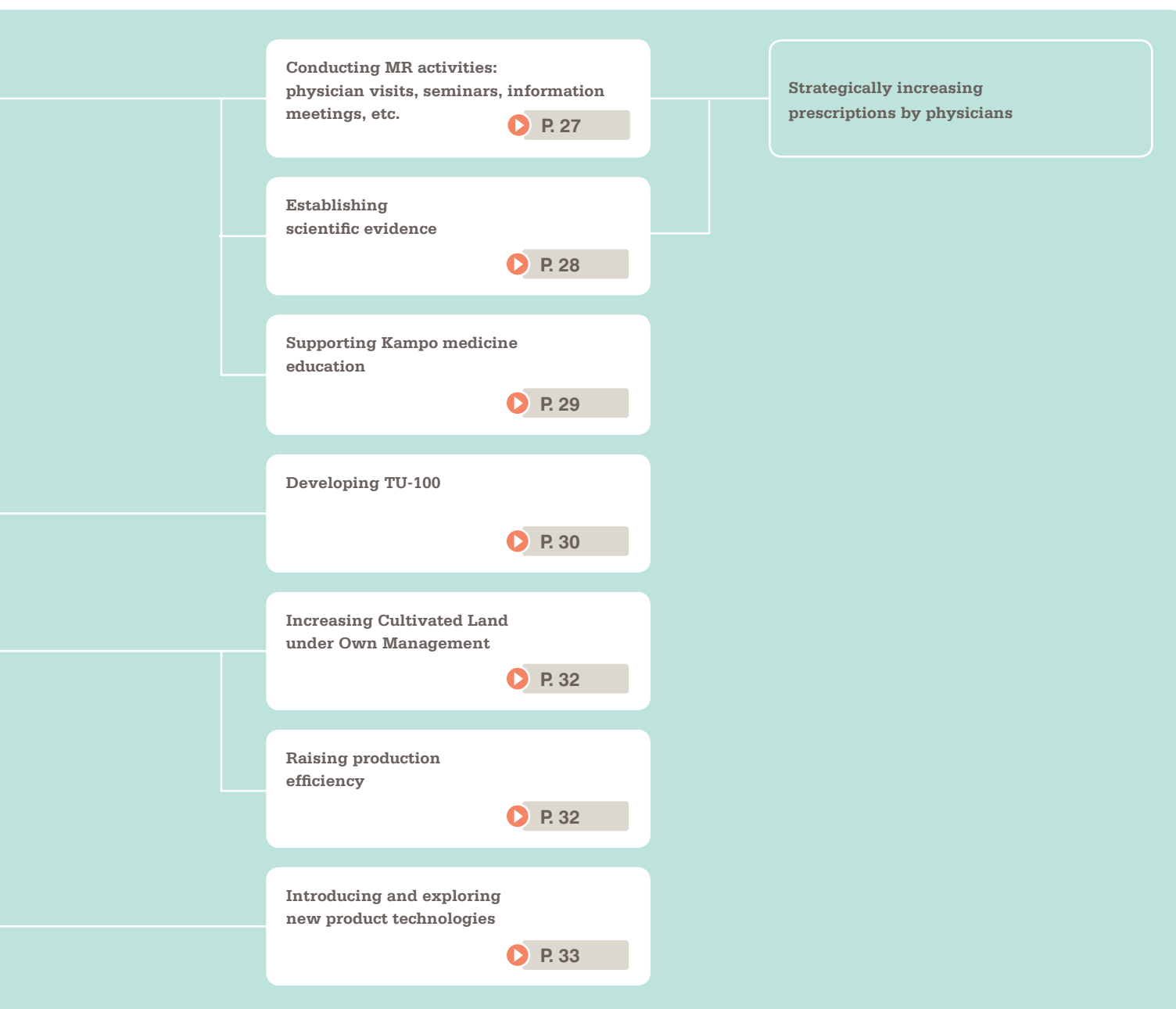
Review of Operations

Guided by its medium-term management plan based on the theme, “Strengthening the growth base to achieve greater value creation,” Tsumura is pursuing three strategic issues—expanding the Kampo medicine market, enhancing earning power, and increasing corporate value by executing effective financial and capital policies.

In the following section, we report on the progress and results of various measures being implemented at each stage of the Kampo value chain regarding the two strategic issues especially related to the Kampo business—expanding the Kampo medicine market and enhancing earning power.



The various measures mentioned in the following section are all measures that Tsumura has been implementing on a long-term basis (see pages 2 and 3). These long-term measures have yielded solid, quantifiable results. Moreover, the accumulation of individual successes and synergies arising from the multitude of positive results have placed Tsumura in a market position unassailable by competitors and led to long-term enhancement in corporate value. Tsumura intends to continue its activities to achieve its long-term business vision, not just this year or for the duration of its medium-term management plan, but for the long term.



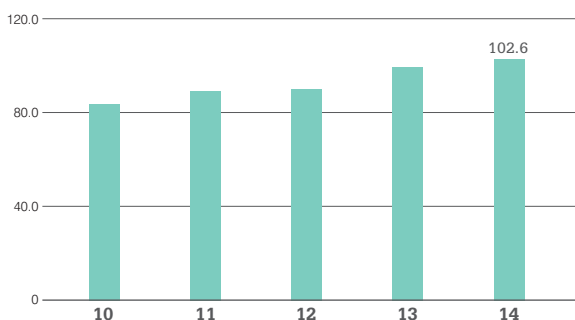
TRENDS IN PHARMACEUTICAL KAMPO PRODUCTS SALES AND PROFITS

Pharmaceutical Kampo Products Sales

In fiscal 2014, the year ended March 31, 2014, net sales increased 4.2% from the previous fiscal year, to ¥110,057 million. Within this amount, sales of the 129 formulations of prescription Kampo products manufactured by Tsumura grew 3.2% from a year earlier, to ¥102,680 million. A total of 66 of the 129 formulations posted year-on-year sales increases.

Sales of Prescription Kampo Products

¥ billion



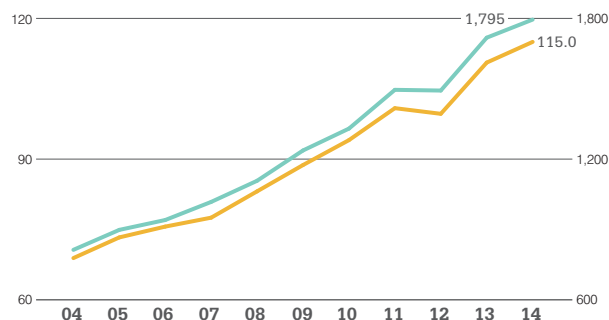
Actual Sales of Prescription Kampo Products

On a unit sales basis, actual sales by pharmaceutical wholesalers to medical institutions climbed 4.5% from fiscal 2013, to 17.95 million units. Sales also increased on a monetary basis, rising 4.0%, to ¥115.0 billion.*¹ As a result, Tsumura's share of the overall market rose to 84.5%.*¹

¹ Copyright 2014 IMS Health. All rights reserved. Estimated based on "IMS JPM Mar. 2014 MAT." Reprinted with permission.

Sales and Quantity of Tsumura Prescription Kampo Products*²

¥ billion / Ten thousands of units



— Sales*¹ — Quantity (right scale)

² Actual sales and quantity: Represent sales and quantity from pharmaceutical distributors to medical institutions

Top 10 Kampo Products by Sales Amount

¥ million

	Product name	Main effectively treatable disorders	FY2014	FY2013	Difference	YoY change
1	TJ-100 (Daikenchuto)	Abdominal pain / abdominal flatulence	9,785	9,094	691	7.6%
2	TJ-41 (Hochuekkito)	Reinforcement of physical strength after illness / anorexia	6,883	6,567	316	4.8%
3	TJ-54 (Yokukansan)	Neurosis / insomnia	6,628	6,041	586	9.7%
4	TJ-43 (Rikkunshito)	Gastritis / maldigestion / anorexia	6,612	6,163	448	7.3%
5	TJ-24 (Kamishoyosan)	Oversensitivity to cold / climacteric disturbance / menstrual irregularity	4,264	4,102	161	3.9%
6	TJ-68 (Shakuyakukanzoto)	Pain accompanying sudden muscle spasms / myalgia or arthralgia / gastric pain and abdominal pain	4,179	3,803	376	9.9%
7	TJ-29 (Bakumondoto)	Coughing / bronchitis / bronchial asthma	3,996	3,879	117	3.0%
8	TJ-107 (Goshajinkigan)	Low back pain / leg pain / numbness / dysuria	3,812	3,783	29	0.8%
9	TJ-114 (Saireito)	Swelling (edema) / acute gastroenteritis	3,343	3,358	(14)	(0.4)%
10	TJ-19 (Shoseiryuto)	Bronchitis / bronchial asthma / rhinitis / allergic rhinitis / allergic conjunctivitis	2,717	2,949	(231)	(7.9)%
—	TJ-14 (Hangeshashinto)	Stomatitis / neurotic gastritis / fermentative diarrhea	1,181	1,120	61	5.5%
Total sales of 129 prescription Kampo products			102,680	99,457	3,223	3.2%

SPECIALIST MEDICAL REPRESENTATIVE ACTIVITIES AND PHYSICIAN NETWORK

Use of Prescription Kampo Products by Physicians

Kampo products are widely used in the healthcare workplace in today's Japan. It is estimated that about 90% of Japan's physicians have prescribed Kampo products for their patients. According to a 2011 survey*³, the average number of different Kampo products prescribed by the respondent physicians who actually prescribe Kampo products was 8.5 products. The figure compares with 7.8 products in a previous survey done in 2008.

³ 2011 Survey on Prescribing Kampo Products, the Japan Kampo Medicines Manufacturers Association

MR Activities

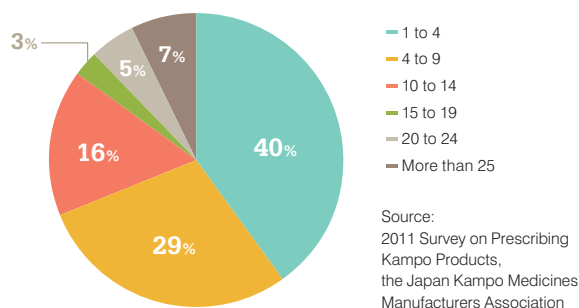
Tsumura is strengthening the marketing approach of MRs for physicians-in-training at designated hospitals for clinical training and university hospitals. For example, the Company is holding Kampo information meetings at designated hospitals for clinical training. In addition, Tsumura is emphasizing follow-up activities, such as holding seminars for practicing physicians in the clinical workplace. There is a high demand for these seminars at medical institutions, and the number of participating physicians is on the rise.

Increase in Physicians Prescribing Kampo Products and in Product Prescriptions

As a result of the Company's MR activities, not only has there been a steady increase in the number of physicians prescribing Kampo products, but also in the number of different Kampo products prescribed. Tsumura plans to continue its marketing activities based on promoting scientific evidence on the efficacy of Kampo medicine through its Kampo medicine seminars. The goal is to increase the number of physicians who prescribe 10 or more Kampo products.

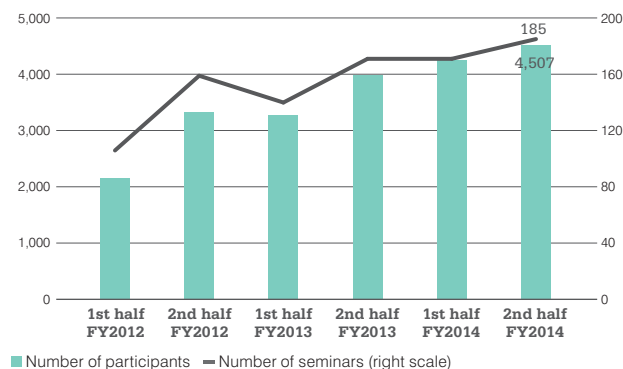
Number of Types of Kampo Products Prescribed by Physicians

Physicians who actually prescribe Kampo products
(Valid number of responses = 558)



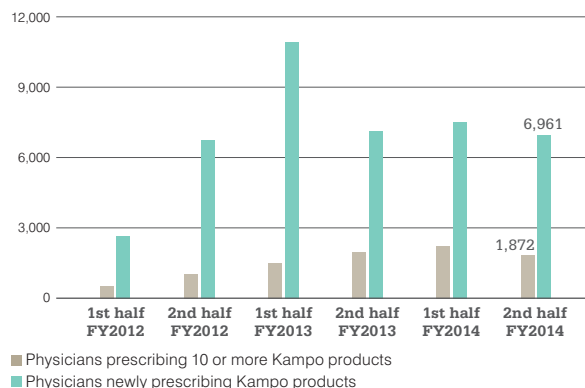
Kampo Medicine Seminars

People / Times



Growth in Physicians Prescribing Kampo Medicine

People



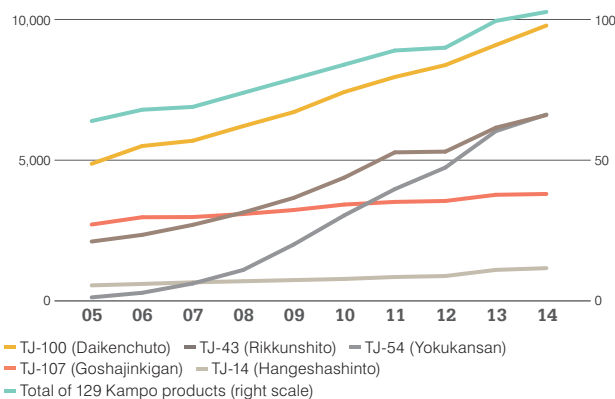
DRUG FOSTERING AND EVOLUTION OF KAMPO PROGRAM PROGRESS

“Drug Fostering” Program Formulation Sales

Building a body of scientific evidence for the five prescription Kampo formulations in the program—TJ-100 (Daikenchuto), TJ-43 (Rikkunshito), TJ-54 (Yokukansan), TJ-107 (Goshajinkigan), and TJ-14 (Hangeshashinto)—is proceeding favorably, stimulating sales growth. In comparison with fiscal 2013, TJ-54 (Yokukansan) took the lead in registering strong year-on-year growth, at 9.7%, followed by TJ-100 (Daikenchuto), at 7.6%, and TJ-43 (Rikkunshito), at 7.3%. TJ-100 (Daikenchuto)'s performance was particularly notable as it posted sales of ¥9,785 million and generated 9.5% of Tsumura's total prescription Kampo products sales.

Sales of “Drug Fostering” Program Formulations

¥ million / ¥ billion

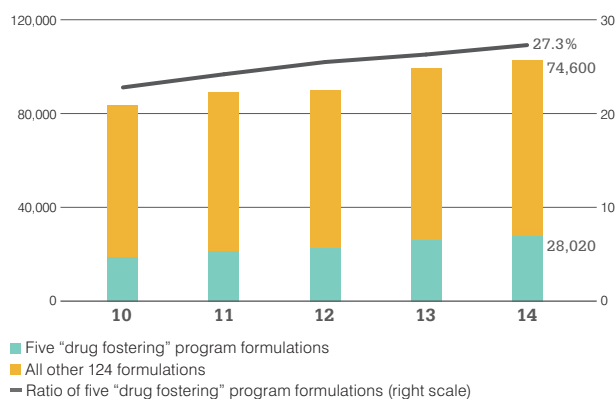


Expanding Sales Contribution of “Drug Fostering” Program Formulations

Driving growth in overall prescription Kampo products, the sales contribution of the “drug fostering” program formulations continues to rise. In comparison with the 3.2% increase in the total sales of Tsumura's 129 prescription Kampo products, sales of the five “drug fostering” program formulations grew 6.9%. As a result, the sales contribution of the five “drug fostering” program formulations rose to 27.3%.

Sales Contribution of Five “Drug Fostering” Program Formulations

¥ billion / %



Five “Drug Fostering” Program Formulations

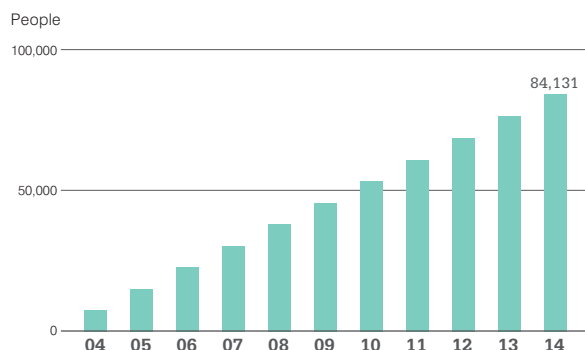
Name	Expected efficacy	Significance to program
TJ-100 (Daikenchuto)	Improves abdominal bloating from illness such as post-operative ileus (intestinal paralysis). Because it has been proven to stimulate or regulate enterokinesis and to increase intestinal blood flow, it is expected to also have application in treating patients with disorders thought to be caused by reduced intestinal blood flow.	Establishing scientific evidence of efficacy of prescription Kampo products in the surgical field.
TJ-43 (Rikkunshito)	Alleviates upper abdominal indefinite complaints arising from functional dyspepsia (FD), gastro-esophageal reflux disease (GERD), and others. Besides helping gastric emptying, it has been reported that TJ-43 (Rikkunshito) improves stomach content retention and helps stimulate the appetite. It is drawing considerable attention for its multiple mechanisms of action (MOA) in sharp contrast to modern drugs.	Elucidating special characteristics of multiple ingredient based Kampo medicine and correlation to MOA.
TJ-54 (Yokukansan)	Improves behavioral and psychological symptoms of dementia such as delusions, hallucinations, anxiety, insomnia, and other disorders.	Researching the medical and economic contribution of Kampo medicine to medicine and medical treatment in an aged society.
TJ-107 (Goshajinkigan)	Alleviates neurotoxicity (numbness) adverse reactions of anticancer drugs and other treatments used in chemotherapy.	Establishing a body of scientific evidence on the efficacy of Kampo medicine in oncology and other advanced medical treatment fields.
TJ-14 (Hangeshashinto)	Mitigates mucosal damage (diarrhea and oral inflammation) resulting from anticancer drugs and other causes.	

ESTABLISHING KAMPO MEDICINE

National Medical Examination as a Symbol of Establishment of Kampo Medicine

Tsumura has been implementing support programs for Kampo medicine education in the belief that having questions on Kampo medicine included in the Japanese national examination for medical practitioners*4 represents a symbol of the establishment of Kampo medicine. In fiscal 2001, the Ministry of Education, Culture, Sports, Science and Technology announced its “medical education model core curriculum,” in which the Ministry included a requirement for Kampo medicine. As a result, Kampo medicine was being taught at all medical schools by fiscal 2005. Currently, 72 of Japan’s 80 medical schools include at least eight Kampo medicine courses in their required curriculum. Consequently, the status of Kampo medicine at medical schools is steadily changing.

Cumulative Total of Physicians Passing the National Examination for Medical Practitioners

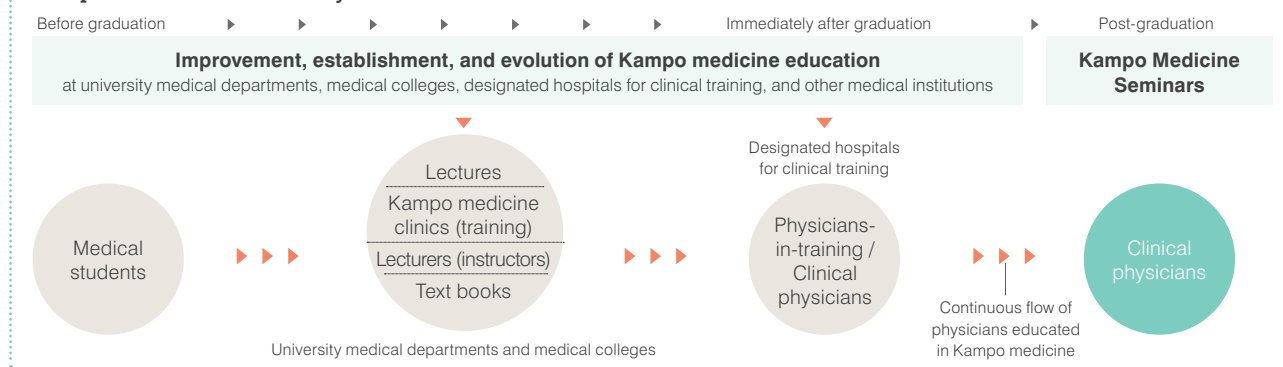


4 Inclusion of questions on Kampo medicine on the national examination for medical practitioners: Currently in Japan, no distinction is made between Western or Kampo medicine under the national licensing system for physicians. However, as yet, there are no questions about Kampo medicine on the national examination.

Major Events Since 2001

- In fiscal 2001, the Ministry of Education, Culture, Sports, Science and Technology announces its “medical education model core curriculum” including an objective of “a general understanding of Japanese Kampo.”
- In fiscal 2002, Tsumura holds its first Kampo Medical Symposium. Since then, the symposium is held annually as a forum for people in the medical education community to discuss Kampo medicine education related issues.
- In fiscal 2005, all medical schools in Japan are teaching Kampo medicine.
- In fiscal 2011, the Ministry revises the “medical education model core curriculum,” upgrading the objective to “a general understanding of Japanese Kampo (Kampo products) and their current uses.”

Kampo Medicine Education System

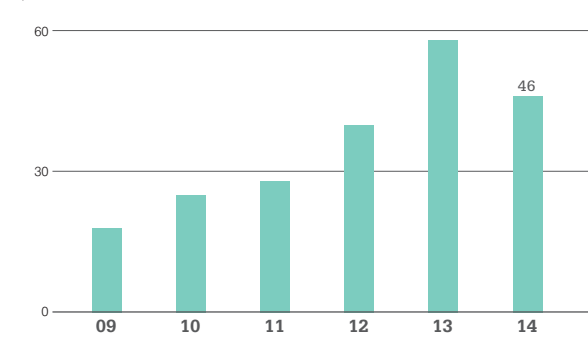


INTERNATIONALIZING KAMPO MEDICINE

Kampo Medicine Related Research Growing

The progress in building a body of scientific evidence on the efficacy of Kampo products has also stimulated heightened interest in Kampo products overseas. There has been a continuous increase in publications in scientific journals on Kampo products. Even at Digestive Disease Week (DDW), the highly regarded gastroenterological conference, there has been a regular inclusion of Kampo medicine related presentations at the annual conference, with 16 such presentations at the 2014 conference.

Kampo Medicine Related Paper Published or Presented
Papers

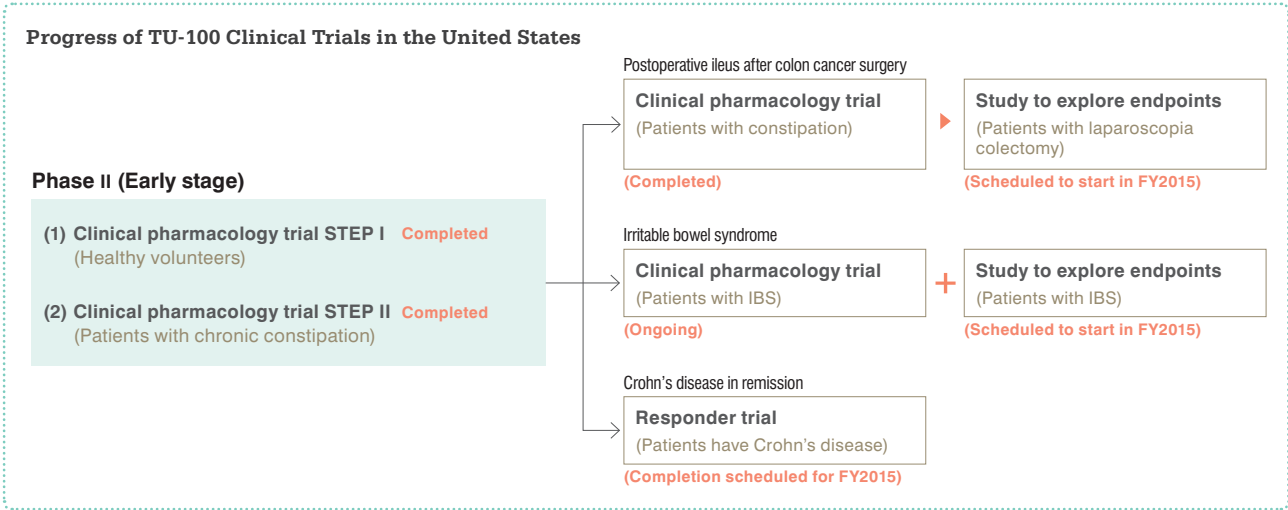


TU-100 (Daikenchuto) Clinical Trials in the United States

Toward its goal of introducing Kampo products to the U.S. market, Tsumura has been proceeding with U.S. clinical trials for TU-100 (Daikenchuto), the product in our “drug fostering” program for which our body of scientific evidence is most advanced. At the same time, through discussions with the U.S. Food and Drug Administration (FDA), we are establishing a scientifically based quality evaluation method for Kampo products and working on meeting quality assurance standards. Our goal is to establish a global standard for botanical drug product quality management.

FDA Approval Process for General Pharmaceuticals

- Investigational New Drug (IND) application
- Phase I to Phase III Clinical Trials
- Preliminary review—New Drug Application (NDA)
- Review Process and Additional Submissions
- Manufacturing Facility Inspection
- New Drug Approval
- Post-Marketing Monitoring



Offering Kampo as Globally Recognized Medicine

Ryuji Takasaki

Managing Director and Executive Officer
Head of Kampo Scientific Strategies Division



For many people the word “Kampo” or “traditional Japanese medicine” conjures up impressions such as “Does it really work?,” “Not effective unless taken long term,” “Mild effect,” “Few adverse drug reactions,” “Unscientific,” and “Mysterious.” Similar conjectures were also brought to light in the hearing survey that Tsumura conducted among U.S. physicians in 2009 before launching its drug development program in the United States. From the survey, the top-ranking information that U.S. physicians wanted to see on Kampo was the same type of information that is generally required for Western drugs (new drugs) including clinical evidence of efficacy, safety data, pharmacokinetics, mechanisms of action, and quality specifications. These are the types of data that are sought out not just by U.S. physicians, but also by Japanese physicians with no experience (or intention) of prescribing Kampo in their clinical practice. Moreover, the U.S. Food and Drug Administration (FDA), which approves pharmaceuticals in the United States, has expressed the need for Tsumura to provide scientific evidence on the efficacy of Kampo on par with that of conventional new drugs.

In 2004, Tsumura began its “drug fostering” program as a part of its decision to concentrate on its core business, the manufacture of Kampo products and cultivation of botanical raw materials. Its strategy is to focus on basic and clinical research of disorders recalcitrant to Western drugs but that show positive results with Kampo products. In other words, this collaborative program is aimed at building a body of scientific evidence on the efficacy of Kampo medicine on the same level as new drug development.

TJ-100 (Daikenchuto) was one of the first three formulations selected for the “drug fostering” program.

With top institutions and surgeons in Japan, Tsumura is conducting basic and applied research, elucidating novel mechanisms of action characteristic to Kampo but inconceivable in modern drugs, one after the other. These research results are provided to healthcare professionals and patients using TJ-100 (Daikenchuto) and disseminated overseas through means such as presentations at international academic conferences and publications in international scientific journals. Furthermore, we have entered an era where not only Japanese researchers but also prominent physicians and research institutions overseas are conducting research on Kampo medicine.

We now have high-quality clinical evidence on the efficacy of TJ-100 (Daikenchuto) through double-blind, placebo-controlled clinical trials conducted at multiple institutions in Japan. Multiple clinical trials are also under way in the United States, with a vibrant exchange of information and resources between Japanese and U.S. physicians.

Tsumura’s investigations have taken basic and clinical research to a whole new level, making progress in such areas as pharmacokinetics studies previously considered difficult to implement, frequency of adverse drug reaction surveys to build safety data, and drug interaction studies. Through these efforts we have successfully tackled and dispelled common misconceptions among physicians and patients regarding Kampo medicine.

Through the internalization of Kampo medicine, we intend to build robust scientific data and facilitate the transition of Kampo products dispensed exclusively in Japan to “Kampo,” a globally recognized traditional medicine from Japan.

STABLE PROCUREMENT OF CRUDE DRUGS AND INCREASING PRODUCTION EFFICIENCY

Procuring Crude Drugs and Expanding Cultivated Land under Own Management

Tsumura is expanding its Cultivated Land under Own Management*⁵ to secure stable procurement of raw material crude drugs in volumes appropriate for the anticipated continued steady growth in demand for Kampo products. Specifically, the Company is planning to increase the ratio of Cultivated Land under Own Management area to total growing area from the current 13% to 33% by March 31, 2017.

5 Farms with a certain scale of cultivation area for which Tsumura directly provides cultivation guidance and has an understanding of cultivation costs and can set procurement prices.

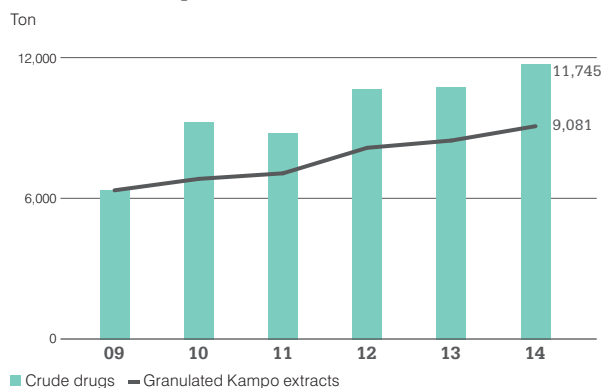
Price Stabilization of Crude Drugs

Because increases in crude drug prices translate directly into higher sales costs, they have a strong impact on profitability. Hence the movement of prices in China, where the Company sources approximately 80% of its raw material crude drugs, is significant. In 2011, the prices for crude drugs spiked in China because of a combination of factors, including growth in crude drug demand, poor weather conditions in the production regions, and speculative investment targeting the situation. Since then, prices have remained high, primarily because of the rise in ginseng prices. Tsumura's policy is to control its procurement prices for raw material crude drugs by expanding its Cultivated Land under Own Management.

Developing Cultivation Technology for Crude Drugs

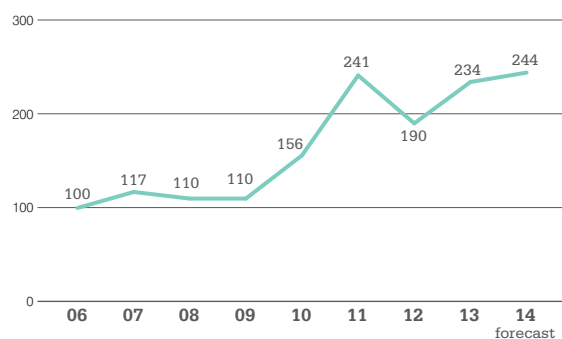
It takes approximately five years to cultivate ginseng, currently the reason for the increased prices for crude drugs. Accordingly, the Company has already concluded a memorandum of understanding (MOU) on joint development of cultivation technology for ginseng with the municipality of Baishan in Jilin Province, China in 2011. Based on the MOU, Tsumura aims to establish a large-scale ginseng cultivation base in the area, expecting that the expanded procurement from the production base will contribute to controlling procurement prices for ginseng.

Amount of Crude Drug Used and Granulated Kampo Extracts Produced



Overall Procurement Price of Crude Drugs Produced in China

Representation of weighted average of actual prices from production region to affiliated company when 2006 price is set as 100



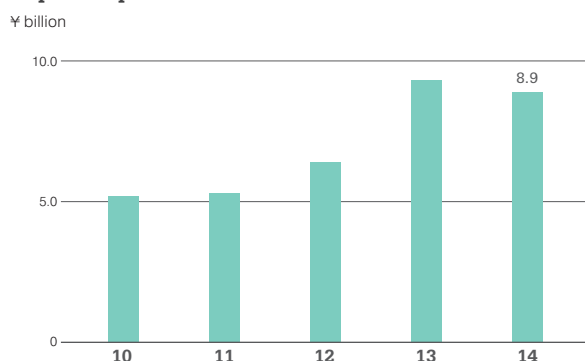
Cultivating ginseng

INTRODUCTION OF NEW MANUFACTURING SYSTEMS

Capital Investment for Sustained Growth

Tsumura is making strategic capital investments to expand production capacity in anticipation of future growth in demand. At the same time, the Company is striving to improve basic productivity through an overall revision of our manufacturing system and the introduction of new manufacturing technology. The overall goal of these efforts is to contribute to a reduction in the sales cost ratio. Furthermore, based on such measures as adjusting the operating system for manufacturing lines and introducing new manufacturing technology, labor productivity rose 7.6% in fiscal 2014 compared with fiscal 2012.

Capital Expenditures



Manufacturing System Innovations

In fiscal 2014, we are proceeding with the construction of new manufacturing systems at home and abroad. Following the October 2013 start of operations of a new powdered extract production method at SHANGHAI TSUMURA PHARMACEUTICALS CO., LTD., we introduced a new granulation system at the Ibaraki Plant, one of our major plants in Japan. The system came on stream in January 2014. At the same time, we also introduced robots and improved energy savings, maintenance systems, and sanitation management.



From insertion into the washer, container rotation, and transfer into the dryer, the whole process is done by robots

Capital Investment Plan

Capital investment to achieve sustained growth

		First Medium-Term Management Plan			Second Plan	
		FY2013	FY2014	FY2015	FY2016	FY2017 and after
Production-related	Shizuoka Plant	Capital investment project				
		New granulation and packaging facilities, etc.				★
		New crude drug warehouse	May			
		SD line-related				★
	Ibaraki Plant	New granulation facility	January			★
Crude drug related		New standard-based facilities, etc.				
	STP (Shanghai)	SD facility	October			
	Production, other	Development / maintenance / renewal				
	Ishioka	Ishioka Center reconstruction	January			
	STM (Shenzhen)	Warehouse	March			
	Yubari	Yubari Tsumura building			★	
	Crude drugs, etc.					

★ Scheduled start of operations

Frequently Asked Questions

Tsumura places high priority on communicating with shareholders and investors, and strives to provide information disclosure that will dispel as much as possible their concerns about the Company and its operations. This FAQ section provides answers to the most commonly asked questions from shareholders and investors received through our investor relations (IR) activities.

Q.

I have heard that prescription Kampo products cannot be patented—does that mean they are something like generic drugs? If that is the case, are there competitive products for Tsumura's formulations?

A.

Prescription Kampo products are really quite different from generic drugs. Moreover, because the barrier to market entry is high, there are a limited amount of competitive products.

Prescription Kampo products are different from generic drugs in that there are no original Kampo products. The reason that there are no patents for prescription Kampo products is that records of their formulation methods have been in existence for 1,800 years, with the formulations and manufacturing methods for many of these products being established and made public in the distant past. In contrast, generic drugs are necessarily premised on the existence of the original drug, and are manufactured and supplied to the market after the patent period has expired.

While competitive products do exist for Tsumura's formulations, it would be jumping to conclusions to think that they are generic drugs for that reason. If we use the example of Kakkonto, often prescribed for the early stages of colds, we would find by comparing the TJ-1 (Kakkonto) manufactured and sold by Tsumura with the Kakkonto of a competitor to have slightly dissimilar crude drug compositions and amounts. These differences arise from the use of crude drugs from different production regions, processing methods for the crude drugs, and other reasons. In that sense, it could also be said that there is no such thing as a generic Kampo product.

The greatest difference between Kampo products and generic drugs is that while Western drugs including generic drugs comprise a single main ingredient, Kampo products are formulated from a mixture of at least two crude drugs, primarily derived from plants. As a result, Kampo products contain multiple ingredients. Manufacturing Kampo products with multiple ingredients as prescription Kampo products requires significant resources and high technology. The raw material procurement network must be capable of delivering crude drugs of a stable and specific quality. In addition, a company must possess advanced technology that can extract the active ingredients with a high degree of concentration consistency from the crude drugs.

Tsumura has accumulated the necessary advanced networks, technologies, and know-how and possesses large-scale storage and manufacturing facilities capable of supporting the manufacturing of a diverse product line extending to 129 prescription Kampo products. These physical and intellectual assets represent a larger barrier to market entry than any patent rights.

Q.

I have heard that the prices for raw material crude drugs are rising in China. Do you expect prices to continue rising and what sort of measures are you taking to control your procurement prices?

A.

Our policy for mitigating the volatility in the market prices is to expand our Cultivated Land under Own Management*¹, particularly in China, but also in Japan and Laos.

There is no doubt that the price for ginseng, which Tsumura uses in 37 of its 129 prescription Kampo products, has continued to increase. Our procurement prices have been rising steadily since 2009, and temporarily spiked in 2011 under the impact of unseasonable weather, speculative attempts to corner the market, and increasing demand. Although prices for ginseng settled down in 2012, they rose to high levels again in 2013.

In the medium to long term, we expect demand for raw material crude drugs to grow in China. It is forecast that China's population will reach more than 1.4 billion in 2030, of which the proportion of elderly people 65 years or older will be 16.2%.^{*2} This aging of China's population in combination with economic growth driven higher incomes should increase demand for medicine. As a result, it is likely that demand for raw material crude drugs in general will continue its upward trend.

The two strategies we are using to deal with these circumstances are to increase our cultivation of crude drugs (please refer to page 36) and our Cultivated Land under Own Management.^{*1} The latter not only allows us to control the quality, production volume, and prices of crude drugs being cultivated, but also mitigate price volatility based on medium- to long-term contracts with the farming cooperatives or local production companies. By expanding our Cultivated Land under Own Management, primarily in China but also in Japan, we plan to increase the ratio of Cultivated Land under Own Management-produced volume to total commissioned volume and the ratio of Cultivated Land under Own Management area to total growing area from 4% and 13%, respectively, at March 31, 2014 to 17% and 33% by March 31, 2017.

1 Farms with a certain scale of cultivation area for which Tsumura directly provides cultivation guidance and has an understanding of cultivation costs and can set procurement prices.

2 Statistics Bureau, Ministry of Internal Affairs and Communications, "World Statistics 2014"
<http://www.stat.go.jp/data/sekai/0116.htm#c02> (only in Japanese)

Q.

The listed drug prices for prescription Kampo products are in a declining trend. Should we expect that there is a high possibility that this trend will continue?

A.

We are making a case for the value of our Kampo products and doing our best to maintain their actual prices, but it is clear that curtailing the decline in prices would require a substantial overhaul of the listed drug price system of the National Health Insurance (NHI) plan.

NHI-listed drug prices are the official prices for pharmaceuticals determined by the Minister of Health, Labour and Welfare. The Ministry regularly revises these NHI-listed drug prices to close the gap between the official drug prices and actual market prices (the prices at which pharmaceutical wholesalers sell to medical institutions). In almost all cases, this means a reduction in the official drug price. As drugs covered by the public health insurance plan, pharmaceutical Kampo products are, in principle, subject to the revision of NHI-listed drug prices once every two years. In the April 2014 revision, the average decline in prices was 3%.

Because of the impact of the previously mentioned upswing in raw material drug prices, Tsumura's sales cost ratio is rising. We are endeavoring to maintain the level of actual market prices by appealing to medical institutions and pharmaceutical wholesalers based on the unique value of the special properties of Kampo medicine. On the other hand, we are also making efforts to control increases in our sales cost ratio by improving productivity. Because the current government policy of steadily reducing official drug prices has the power to offset our management efforts, however, we take a great interest in the possibility of revising the system. Through our participation in the Japan Kampo Medicines Manufacturers Association (JKMA), we are carrying out lobbying activities recommending such a future revision.

Research and Development

Through its R&D activities, Tsumura is actively seeking to elucidate the mechanisms of Kampo products that have a history of use reaching back 1,400 years. The Company's purpose is to establish Kampo medicine as a useful contributor to modern medicine.

Basic R&D Policy

The most important area being addressed by Tsumura R&D programs is the establishment of a body of scientific evidence for the efficacy of pharmaceutical Kampo products. Previously, the Company's drug discovery programs focused on Western drugs similar to other pharmaceutical companies. However, in 2004, Tsumura halted these programs and shifted the direction of its R&D policy to concentrate its resources on the accumulation of a body of evidence for existing Kampo products. The backdrop to this action was a determination by management that for the Company to achieve its mission of "contributing to the unparalleled medical therapeutic power of the combination of Kampo medicine and Western medicine," it had to put Kampo products on the same playing field as Western drugs. In other words, Tsumura recognized that Kampo medicine would only truly be accepted as a Japanese form of medicine when its efficacy could be demonstrated using the same logic as applied to Western medicine—a scientific body of evidence.

Establishing a Body of Evidence

Guided by the new R&D policy, Tsumura is concentrating its research efforts on five formulations in its endeavor to establish a body of scientific evidence for the efficacy of Kampo products. Taking into consideration the recent structure of disease, the Company is targeting prescription Kampo products that demonstrate special efficacy in patients with disorders for which the use of new drugs is difficult or for which there are strong medical needs. In addition to gathering basic data through its own research, Tsumura is building a collaborative R&D network by supporting the work of medical research specialists that gather and analyze basic and clinical data.

For one of the five formulations mentioned previously, Tsumura has implemented a program to develop the formulation as a prescription drug for the U.S. market and launch it (please refer to page 30). The Company is working to

achieve efficient R&D in the program by linking its results in Japan with its development drive in the United States.

Contributing to the Kampo Value Chain

One of the research areas of Tsumura's R&D program is solving issues related to the Kampo value chain. These activities directly contribute to advancing the sophistication of the Kampo value chain and to increasing Tsumura's corporate value. The three main research themes in this area are (1) researching cultivation technology to secure stable supplies of raw material crude drugs, (2) enhancing the quality of raw material crude drugs, and (3) improving Kampo product quality control and manufacturing technology.

In the case of researching cultivation technology, the Company's efforts over more than 10 years have borne fruit in terms of the successful establishment of cultivation technologies for licorice and ephedra herb. As rare species, the Chinese government has restricted exports of both licorice and ephedra herb grown in the wild. Therefore, the shift to cultivated forms will have an extremely large impact on the stable procurement of raw material crude drugs for Tsumura.

Similarly, because of the concern about soaring prices for ginseng (please refer to page 34), Tsumura concluded a memorandum of understanding with the municipality of Baishan in Jilin Province, China in 2011, and is proceeding with joint development of cultivation technology for ginseng. Baishan is a major production area for ginseng in China. Through the provision of cultivation, quality control, and production management knowledge and technology, Tsumura aims to establish a large-scale ginseng cultivation base here.

Quality control for Kampo products is an important issue throughout the Kampo value chain. Accordingly, Tsumura implements various measures at each stage of the chain. At the cultivation and procurement stage, the Company provides guidance to farmers on cultivation technology. In addition, Tsumura has developed technology to differentiate all crude drugs on a DNA level. The procured raw material

Kampo Efficacy Scientific Evidence (DB-RCT & Safety)

Formulation	Targeted disorder	Institution in-charge	Trial collection period	Public announcements, etc.
TJ-100 Daikenchuto	Postoperative ileus after liver cancer surgery	Tokushima University, other 30 institutions	End of trial	Published in International Journal of Clinical Oncology
	Postoperative ileus after colon cancer surgery (main trial)	Kitasato University, other 64 institutions	End of trial	Paper submission in preparation
	Postoperative ileus after colon cancer surgery (supplemental trial)	Fujita Health University, other 19 institutions	End of trial	Paper submission in preparation
	Postoperative ileus after gastric cancer surgery	Oita University, other 43 institutions	End of trial	Adopted for DDW* 2014 / paper submitted
	Paralytic ileus after pancreatic cancer surgery; JAPAN-PD Study	Wakayama Medical University, other 10 institutions	Analysis proceeding	—
	Crohn's disease in remission	Keio University, other 9 institutions	– Mar. 2015	Case collection ongoing
	Gastrointestinal dysfunction after liver transplant; DKB-14 Study	Kyoto University, other 14 institutions (scheduled)	June 2014 – May 2016	Case collection ongoing
TJ-54 Yokukansan	Intractable schizophrenia	Shimane University, other 33 institutions	End of trial	Paper submitted
	Intractable schizophrenia (long-term trial)	Shimane University, other undecided	Fiscal 2015 – Apr. 2016	Scheduled to start in fiscal 2015
	BPSD	Tohoku University, other 21 institutions	End of trial	Paper submitted
TJ-43 Rikkunshito	Intractable gastroesophageal reflux disease; G-PRIDE Study	Osaka City University, other 75 institutions	End of trial	Published in Journal of Gastroenterology
	Functional dyspepsia (FD); DREAM Study	Osaka City University, other undecided	Apr. 2014 – Mar. 2016	Case collection ongoing
	Functional dyspepsia (FD); gastroesophageal reflux (GER) clinical pharmacological trials	University of Leuven	Oct. 2014 – Mar. 2016	Scheduled to start in Oct. 2014
TJ-107 Goshajinkigan	FOLFOX treatment peripheral neuropathy; GONE Study	Asahikawa Medical University, other 16 institutions	End of trial	Published in Cancer Chemotherapy and Pharmacology
	FOLFOX treatment peripheral neuropathy; GENIUS Study	Kyushu University, other 43 institutions	Trial halted (May 2012)	—
TJ-14 Hangeshashinto	Oral inflammation from chemotherapy for colon cancer; HANGESHA-C Study	National Hospital Organization Osaka National Hospital, other 18 institutions	End of trial	Paper submitted
	Oral inflammation from chemotherapy for stomach cancer; HANGESHA-G Study	Kanagawa Cancer Center, other 14 institutions	End of trial	Published in Cancer Chemotherapy and Pharmacology
TJ-54 Yokukansan	Frequency investigation of adverse drug reactions	—	Oct. 2012 – Mar. 2014	Analysis proceeding
TJ-68 Shakuyakukanzoto	Frequency investigation of adverse drug reactions	—	Oct. 2013 – Sept. 2014	Research ongoing

* Digestive Disease Week

crude drugs are tested for residual agricultural chemicals, microorganisms, and heavy metals at SHENZHEN TSUMURA MEDICINE in China and at the Analytical Technology Center in Japan. The Company has developed new analytical methods that cover all of the agricultural chemicals that are used in the cultivation of crude drugs in Japan and China. Using analytical results, the Company manages the quality of its raw materials.

Quality remains an important focus at the manufacturing stage as well, with Tsumura complying with GMP* and Kampo GMP standards for manufacturing and quality control. The Company constantly endeavors to improve its manufacturing technology (please refer to page 33).

* Good Manufacturing Practice: Manufacturing standards set by the Minister of Health, Labour and Welfare as stipulated in the Pharmaceutical Affairs Act.

Creating Shared Value

SHARED VALUE OF CRUDE DRUG PROCUREMENT AND AGRICULTURAL VITALIZATION

Tsumura's procurement of crude drugs is based on cultivation contracts with cultivation cooperatives and organizations. The following article reports on the significance of Tsumura's procurement activities for the region and the farmers based on the relationship of trust built over the years from the farmer's point of view.

Thirty-Nine Years Under Contract to Tsumura

In Iwate Prefecture, the Iwate Medicinal Herb Producers' Association's cultivation of crude drugs began in 1975 based on a contract with Tsumura. In fact, it was the first producers' association in Japan to make a contract with Tsumura. The Company was preparing for the growth in demand that would result from the inclusion of 33 of Tsumura's formulations on the NHI Drug Price List for the first time in 1976. The stable procurement of raw material crude drug has been one of Tsumura's top management priorities since those days.

At that time, production of leaf tobacco was flourishing in the region, but there were signs that demand for leaf tobacco would probably decline in the future. In actual fact, the farming land under leaf tobacco cultivation has continued to fall from the 1970s to the 2010s. It looks like the shift to crude drug cultivation has contributed to the sustainability of farming in the region. Looking back on the growth of the producers' association, its president Maiko Iwai recalls, "When the association was first set up 39 years ago, there were only a few members, but as of 2014 we have about 217 members."

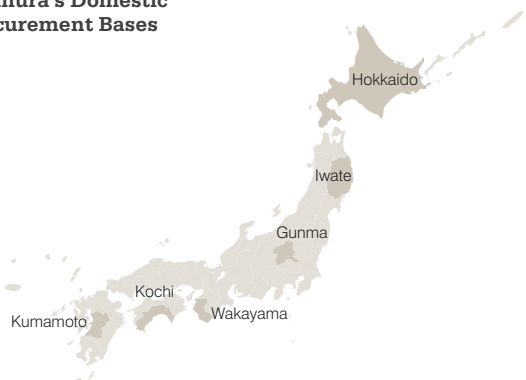


Iwate Medicinal Herb Producers' Association president Maiko Iwai talks about her hopes of spreading interest in crude drug cultivation among the younger generations.

Stable Income is the Advantage of Crude Drug Cultivation

Ms. Iwai continues, "The reason our association has grown to this size is clearly because crude drug cultivation offers many advantages to farmers. The best thing about it is that they give you stable income. We grow products other than crude drugs, such as asparagus and blueberries, but the prices of those types of products fluctuate with the weather, season, and demand. It is unsettling to grow a crop not knowing how profitable it is going to be. In that sense, the cultivation of crude drugs allows you to figure out your income because of the contract with Tsumura." Shuichi Fugane, a member of the association who decided to cultivate crude drugs based on his acquaintance with someone else growing it, says, "Agriculture is the lifeblood of the economy of Iwate-machi. I believe that the more the farmers and agricultural industry thrive, the more the town will thrive. That's why I am aiming to make crude drug cultivation my business."

Tsumura's Domestic Procurement Bases



Crude Drug Cultivation Requires Relatively Less Physical Strain

Association member Toshi Katabira also is happy about her work. “I feel motivated to be growing a crop that becomes the raw material for medicine and helps people. The nice thing about the perilla that I grow is that it can be harvested quickly because it has a short growing period of about six months.” The growing periods for crude drugs vary according to species, but the perilla, don quai, and cnidii rhizoma cultivated by the Iwate Medicinal Herb Producers’ Association all can be harvested after relatively short growing periods. Ms. Katabira says, “I’m over 80 years old so my son helps me with the reaping anyway, but the crude drugs are not heavy and put less physical strain on me. Another helpful quality of crude drug cultivation is that we dry the crop immediately after harvesting it, so it doesn’t have to be shipped immediately after harvesting like vegetables.”



Association member Toshi Katabira explains that one of the advantages of crude drug cultivation is that it is physically easier work than vegetable farming.



Weeds and Disease Are Deadly Foes, but We Put in the Hard Work to Raise Crops

Because of their role as raw materials for pharmaceutical Kampo products, the types and amounts of agricultural chemicals, fertilizer, and other growing aids are managed extremely strictly. “While we can use herbicides on other agricultural crops, Tsumura has strict standards on the use of agricultural chemicals with crude drug crops, so in a sense, cultivating crude drugs means a constant battle with weeds,” says Ms. Iwai with a frown. “Protecting against disease is also hard. However, firm cultivation management is not reserved only for crude drugs, is it—before growing crude drugs, I managed cows on a stock farm for 30 years. Putting in the hard work to raise them is the same for cows and crude drugs,” says Ms. Iwai, with a smile. Ms. Iwai is the first women president of the Iwate Medicinal Herb Producers’ Association. She says, “Of course, it’s hard work being responsible for 217 members as the association’s president. But it makes me so happy to see the vitality of the association, which includes retired people who still put a real effort into raising crude drugs as well as young people who are eager to work after having returned home from working in the major cities of Japan—I’ve already served as president for six years.” Mr. Fugane is also enthusiastic about his job. “Since there is no fixed manual on crude drug cultivation, I find it interesting to think up ideas to improve processes so the job motivates me. I think you have to be brave in proactively trying out new methods to achieve high yields,” he says.



Association member Shuichi Fugane works hard every day to make crude drug cultivation a successful business.

Town Also Supporting Crude Drug Cultivation

Ms. Iwai’s hope is that Iwate-machi will develop into a crude drug production region. She says, “Because crude drug cultivation has a future, the Iwate-machi Town Hall has also started up a ‘Become a Production Region Project.’ A movement intending to drive the further expansion of crude drug cultivation as a local business is underway through such actions as financial assistance from the town hall and the loan of machinery by Tsumura to help us improve our cultivation efficiency. Over the past few years, we have made progress with the mechanization of weed removal, making the production process much easier. Bringing in more young people as producers, I want to expand crude drug cultivation in our region.”

“Contract-based crude drug cultivation is highly appealing because it offers a stable source of income. Knowing your probable income makes it easy to plan for the future, an advantage that attracts motivated producers.”

—Ms. Iwai, President of the Iwate Medicinal Herb Producers’ Association

Crude Drug Cultivation in Laos Supports Regional Residents as well as Farmers



LAO TSUMURA's Inthaphone Phimmathong's eyes brighten when he talks about how enjoyable it is to work with the special crude drug cultivation machinery.

Tsumura established LAO TSUMURA CO., LTD., in Laos in 2010.

The purpose was to strengthen the traceability system for its crude drug procurement network and achieve stable production of crude drugs through the use of Cultivated Land under Own Management. Because LAO TSUMURA, through its business operations, is creating jobs locally and contributing to the establishment of social infrastructure, such as building roads and bridges, the government of Laos has high expectations for LAO TSUMURA to contribute to the development of the region. Including its local staff of 51, the subsidiary employs a total of 120,000 local farmers as agricultural workers.

Joining LAO TSUMURA in 2011, and currently the manager of the crude drug production department, Inthaphone Phimmathong talks about the benefits to the local community. "Thanks to LAO TSUMURA, many local people who had to travel long distances outside the local area to find work can now earn a stable income right here at home. I feel that we are supporting the overall lives of residents because in addition to our cultivation business we are building infrastructure," says Mr. Phimmathong.

Since he spent three years in Japan doing agricultural training, working at LAO TSUMURA represents the perfect opportunity for Mr. Phimmathong to make use of his experience. He says, "Crude drug cultivation has its difficulties, such as the great deal of manpower required. However, having to constantly come up with creative ideas on how to improve the cultivation method or technology to reach our annual production goals motivates me. I want to become a crude drug cultivation expert who can solve the many crude drug cultivation problems that other farms are facing."

Supported by such enthusiastic employees, LAO TSUMURA is contributing to the local community in the operation of its business.



Creating Shared Value

TJ-54 (Yokukansan) and Dementia Care

It is known that TJ-54 (Yokukansan), one of our five “drug fostering” program formulations, is effective in treating nervous disorders associated with the behavioral and psychological symptoms of dementia (BPSD). Dementia presents two sets of symptoms, central nervous systems disorders, such as memory impairment, and BPSD, such as delusions, hallucinations, insomnia, wandering, and other disorders. Dealing with the language and behavior problems associated with BPSD is a heavy burden for caregivers.

BPSD has been treated with Western drugs, but there have been more than a few cases where the adverse reactions of the drugs made continued treatment with drugs difficult. On the other hand, it has been proven that TJ-54 (Yokukansan) mitigates anger and over-excitement, improving BPSD symptoms. This results in a substantial reduction of the burden on the caregivers.

As of 2012, the proportion of people with dementia among the elderly in Japan 65 years old or more was 15%, or approximately 4,620,000 people. This works out to about one in seven people 65 years or older having dementia.*¹ As the population continues to age, it could be said that care for dementia patients will be one of the demands placed on our society. Tsumura is assisting with dementia treatment through the benefits of care using TJ-54 (Yokukansan), which contributes to not only improving the symptoms of the patients, but also alleviating the burden of the family and the caregivers.

¹ Health and Labour Sciences Research Grants (General Research on Measures against Dementia), “The Proportion of People with Dementia in Cities and Measures for Dealing with Dementia’s Daily Living Functional Disorders,” March 2013.

Employment of People with Disabilities in Crude Drug Cultivation Operations

In fiscal 2010, Tsumura established a three-year employment plan to create job opportunities for people with disabilities on a Groupwide basis. Since then, the Group has consistently worked to increase the percentage of people with disabilities in its workforce. As a result, that percentage had risen to 3.75% at the March 31, 2014, remaining well above the 2.0% legal employment percentage for people with disabilities set by the Japanese government.

Tsumura is emphasizing creating job opportunities for people with disabilities in our crude drug cultivation operations. In April 2010, our subsidiary YUBARI TSUMURA CO., LTD., signed a contract with Temiru Farm*² commissioning them to cultivate crude drugs. Through this agreement, we are creating jobs for people with disabilities, giving them an opportunity to get involved with cultivating crude drugs. Harunire No Sato Plant Manager Hidetoshi Ikeda sums up the success of the program, “For people with disabilities, knowing that the crude drugs they are producing will become medicine for others gives them a huge sense of achievement—the job is an important place where we can participate in society.”

Since fiscal 2012, in addition to crude drug cultivation, YUBARI TSUMURA has also begun producing seedlings for the purpose of increasing yields and stabilizing quality. Going forward, Tsumura intends to continue to find ways of creating jobs for people with disabilities in its cultivation operations.

² An agricultural production corporation established in April 2010 by Harunire No Sato, a social welfare corporation based in Hokkaido with 50 offices and facilities in Sapporo and Ishikari, for the purpose of helping people with mental disabilities to become more independent.



Corporate Governance

Basic Policy

Tsumura positions corporate governance as one of its most important management issues. We do so in recognition that further strengthening our corporate governance organization is essential to achieving sustained growth and development as well as fulfilling our social responsibilities based on our corporate philosophy of “the Best of Nature and Science.”

The Company has introduced a corporate officer system to clearly separate the oversight role of directors and the operational execution role of corporate officers as well as to establish a management organization that can respond quickly to changes in the business environment.

Board of Directors and Auditors

Name	Title	Appointed director	Shareholdings (thousands of shares)
Terukazu Kato	President & Representative Director	June 2011	9.0
Toru Sugita	Senior Managing Director, Executive Officer	June 2007	14.1
Ryuji Takasaki	Managing Director, Executive Officer	June 2012	4.7
Shuichi Takeda	Director, Executive Officer	June 2010	6.9
Terunari Nakayama	Director, Executive Officer	June 2011	9.8
Yasunori Fuji	Director, Executive Officer	June 2011	15.6
Tsuyoshi Iwasawa	Director, Executive Officer	June 2012	9.2
Shigeru Sugimoto	Outside Director Certified Public Accountant/Certified Real Estate Appraiser/Certified Tax Accountant Representative, Sakura Horwath Audit Corporation	June 2012	0.6

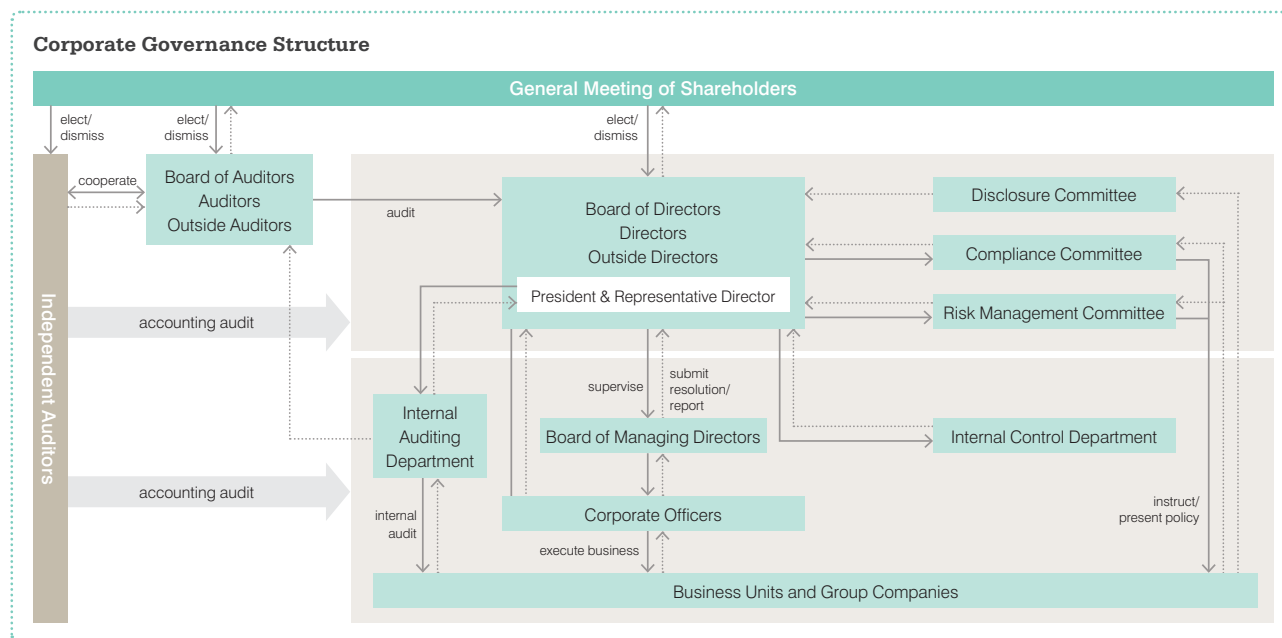
Name	Title	Appointed auditor	Shareholdings (thousands of shares)
Yoshiki Mori	Auditor	June 2011	12.6
Yukio Minato	Auditor	June 2011	5.2
Tomiji Yusa	Outside Auditor Certified Public Accountant (Japan and New York) Chief Executive Officer, Mercury Financial Brain Co., Ltd. Corporate Auditor, Aoi Advertising Promotion Inc.	June 2007	2.5
Seiko Noda	Outside Auditor Lawyer Partner, Nagasawa Law Offices	June 2007	2.2

Director Compensation

Category	Total compensation (¥ in millions)	Breakdown of total compensation				Number of directors compensated
		Basic	Stock options	Incentive	Severance	
Directors (excluding outside directors)	496	496	—	—	—	9
Auditors (excluding outside auditors)	47	47	—	—	—	2
Outside directors and outside auditors	24	24	—	—	—	3

Overview of Corporate Governance System

- Board of Directors**
 As management's top decision-making body, the Board of Directors makes decisions related to law, the articles of incorporation, and other important matters regarding Tsumura's business as well as overseeing business execution.
 Number of directors: 8 (including one outside director)
- Board of Managing Directors**
 The Board of Managing Directors discusses important issues to determine general operational policies based on the fundamental policies set by the Board of Directors. Also, the Board of Managing Directors exercises overall control of business operations.
 Number of board members: 3
- Corporate Officers**
 Appointed by the Board of Directors, corporate officers manage and execute the operations they are given responsibility for.
 Number of corporate officers: 10
 Officers who are also directors: 6
- Board of Auditors**
 The Board of Auditors, comprising all appointed auditors, determines auditing policies based on the Board of Auditors' regulations, pertinent laws, and Tsumura's articles of incorporation. Also, the Board of Auditors forms its audit opinion by integrating all auditor reports.
 Number of auditors: 4 (including two outside auditors)
- Auditors**
 Auditors monitor the decision-making processes of the Board of Directors and the Board of Directors' execution of business operations by attending Board of Directors meetings and other important meetings, holding periodic meetings with the members of the Board of Managing Directors, reviewing documents related to important decisions, and, as necessary, conducting hearings with directors and corporate officers on business operations. Auditors periodically receive reports from the Internal Auditing Department and meet with them to exchange opinions. As necessary, the auditors are present during the internal audits or take other collaborative measures.
- Independent Auditors**
 The independent auditors and the Board of Auditors meet periodically to exchange opinions and to share information regarding relevant issues.



Strengthening Corporate Governance

Appointment of Outside Director

Commencing with the fiscal year ended March 2013, Tsumura decided to place an outside director on the Board of Directors for the first time. The Company took this action in order to strengthen its board of directors' oversight function to increase its competitiveness and corporate value.

Tsumura judged that the new outside director, Mr. Shigeru Sugimoto, would adequately fulfill his role in making decisions about the important business matters of the Company and in providing oversight of the execution of operations. Tsumura made that decision based on the fact that Mr. Sugimoto has acquired a wealth of experience and knowledge in his careers as a certified public accountant (CPA), certified real estate appraiser, and certified tax accountant as well as being involved with business management as the representative of several companies. By having a person knowledgeable about management of a business other than Tsumura's business participate in the Company's management from an independent perspective, Tsumura is aiming to further vitalize the discussion of the Board of Directors and strengthen the management oversight function. Going forward, the Company will endeavor to constantly reinforce its corporate governance, maintain management transparency, and increase corporate value.

Appointment of Outside Auditors

As a firm that has chosen to be a company with auditors under Japanese law, Tsumura has four corporate auditors to provide business auditing and management oversight. The Company has chosen a lawyer and a CPA as its two outside auditors.

Mr. Tomiji Yusa is a CPA and has a considerable amount of knowledge of finance and accounting. He has been asked by the Company to serve as an outside auditor to lend his abundant experience and insight as a CPA to Tsumura's auditing operations.

Ms. Seiko Noda has been asked by the Company to serve as an outside auditor to lend her expertise as an attorney to Tsumura's auditing operations.

As highly independent specialists, Tsumura feels that its two outside auditors ensure the objectivity and neutrality of its management oversight function.

Message from the Outside Director by Shigeru Sugimoto

It has been two years since I became an outside director of TSUMURA & CO. Thanks to the thoughtful explanations of those responsible for business operations and two inspection tours of Tsumura's Ibaraki and Shizuoka plants, I am gradually coming to understand the company's manufacturing processes for pharmaceutical Kampo products.

In comparison with other companies, I would say that Tsumura is unique in both its profit structure and the business issues it faces. In the board of directors meetings, among others, I have asked questions on accounting procedures and inventory evaluation methods based on interest stemming from my area of expertise. While I still do not fully understand some of the finer points of Tsumura's manufacturing technology and other aspects of the business, I proactively offer my opinions on the issues being discussed. I do so with the belief that my mission is to provide opinions from a different mindset than Tsumura's people, keeping in mind shareholder concerns as to whether the business is being run properly.

If I think back, I have been given a great deal of latitude to express my opinions ever since I became the first outside director to sit on Tsumura's board of directors. As a director of a company with a corporate culture that encourages unrestricted factual debate, I plan to contribute to increasing corporate value by asking questions and offering opinions that are constructive in nature.

Corporate Governance

Corporate Governance Activities

Item	Details
Corporate structure	Company with auditors under Japanese law
Chairman of board of directors	Director without an executive position
Annual number of board of directors meetings	19 times
Board of directors meetings attended by outside director	19 times
Annual number of board of auditors meetings	25 times
Board of auditors meetings attended by outside auditors	Mr. Tomiji Yusa (25 times) Ms. Seiko Noda (25 times)
Board of directors meetings attended by outside auditors	Mr. Tomiji Yusa (19 times) Ms. Seiko Noda (19 times)
Audit corporation	Ernst & Young ShinNihon LLC
Audit corporation compensation	¥45 million

Other Management Systems

Item	Details
Compliance	<p>The Company formulated the Tsumura Compliance Program, including the Tsumura Code of Conduct, as the basic business practice rules for compliance in its business activities. Based on this program, the Company is carrying out continuous and systematic compliance activities, including educating relevant stakeholders.</p> <p>The director in charge of compliance (director in charge of the Compliance Advancement Department) keeps track of Companywide efforts and regularly reports on them to the Board of Directors. Group compliance policies are determined by the Board of Directors.</p> <p>To promote compliance, the Company has established a hierarchy of compliance staff—the Chief Compliance Officer, a director in charge of compliance, compliance officers, compliance supervisors as well as the compliance office (Compliance Advancement Department). These compliance-related employees and sections are responsible for establishing the Group's overall compliance system, educating employees about it, and spreading its use. In addition, they implement activities to promote the observance of corporate ethics.</p>
Internal Control	<p>On April 1, 2013, the Company established an Internal Control Department for the purpose of strengthening the overall Group internal control system.</p> <p>The Company has established the Disclosure Committee to boost its information disclosure efforts based on strengthening its internal control system for information disclosure. The purpose of the committee is to consider appropriate information disclosure based on relevant laws and regulations and to increase the quality and transparency of information disclosure by clarifying the responsibility of those involved.</p>
Risk Management	<p>The Company has decided basic guidelines regarding risk management by the Group and created the Risk Management Rules to support their effective implementation.</p> <p>The Company has built an organization to promote risk management, including a Chief Risk Management Officer, a director in charge of risk management, a Chief Risk Compliance Officer, risk compliance officers, and the risk management office (General Affairs Department). The Company has also established systems for setting up internal risk management systems, for determining and evaluating business risks, for taking measures to avoid the occurrence of risk events, and for minimizing damages and losses should a risk event occur.</p> <p>If an emergency situation occurs that threatens to have a serious impact on the business operations of the Group, the Chief Risk Management Officer has the authority to establish an emergency crisis management office with himself as senior manager and implement measures to resolve the crisis.</p> <p>The Board of Directors is kept informed of the overall status of risk management within the Tsumura Group through regular reports by the director in charge of risk management (director in charge of the General Affairs Department).</p>

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FINANCIAL SECTION
Eleven-Year Selected Financial Data (Unaudited)

TSUMURA & CO. and subsidiaries
Years ended March 31

¥ in million

	2014	2013	2012
For the year			
Net sales	¥110,057	¥ 105,638	¥ 95,450
Cost of sales* ¹	38,787	35,927	29,944
Gross profit	71,269	69,711	65,505
Selling, general and administrative expenses	48,808	46,586	44,271
Operating income	22,461	23,124	21,233
Income before income taxes and minority interests	28,118	24,062	22,448
Net income	18,050	15,373	13,431
At year-end			
Inventories	¥ 43,424	¥ 35,565	¥ 30,570
Property, plant and equipment, net	57,148	50,657	44,869
Long-term liabilities	9,126	9,448	8,093
Total liabilities	54,305	51,929	49,633
Total net assets* ²	133,318	118,537	102,240
Total assets	187,623	170,466	151,874
Other selected data			
Capital expenditures for property, plant and equipment	¥ 8,991	¥ 9,328	¥ 6,425
R&D expenses	5,949	4,904	4,565
Depreciation	4,871	4,049	3,850
Free cash flow	4,214	3,988	1,972
Cash flows from operating activities	5,908	12,011	7,314
Cash flows from investing activities	(1,694)	(8,022)	(5,342)
Cash flows from financing activities	(4,575)	(4,275)	(5,272)
Cash and cash equivalents, end of year	14,418	13,762	13,906
Per share data (yen)			
Net income	¥ 255.94	¥ 217.98	¥ 190.45
Dividends	64.00	62.00	60.00
Net assets* ²	1,860.14	1,658.88	1,430.94
Financial ratios (%)			
As a percentage of net sales:			
Gross profit	64.8%	66.0%	68.6%
Selling, general and administrative expenses	44.3	44.1	46.4
Operating income	20.4	21.9	22.2
Income before income taxes and minority interests	25.5	22.8	23.5
Net income	16.4	14.6	14.1
ROE	14.5	14.1	14.1
ROA	12.5	14.3	14.5
Current ratio	240.6	222.5	207.8

¹ Including credit (debit) for allowance for sales returns.

² Due to a change in accounting standards, figures for the fiscal year ended March 2006 and prior years are net shareholders' equity.

	2011	2010	2009	2008	2007	2006	2005	2004
	¥ 94,778	¥ 90,933	¥ 90,016	¥ 94,799	¥ 91,227	¥ 90,419	¥ 84,837	¥ 82,155
	29,435	28,518	29,028	31,609	29,438	28,000	26,522	25,635
	65,342	62,414	60,987	63,190	61,788	62,419	58,314	56,520
	43,789	43,475	44,504	47,369	46,282	45,951	46,351	45,298
	21,553	18,938	16,483	15,820	15,505	16,467	11,962	11,221
	21,058	18,710	17,940	14,605	21,261	14,726	8,548	9,132
	12,945	10,704	10,777	9,139	13,152	12,380	10,401	8,479
	¥ 22,057	¥ 22,335	¥ 19,810	¥ 19,651	¥ 17,073	¥ 16,468	¥ 15,655	¥ 15,842
	42,154	40,857	38,754	40,251	41,289	48,497	47,702	49,219
	8,587	8,773	8,970	14,440	21,400	26,287	32,354	39,836
	50,394	50,944	52,855	62,734	73,760	79,482	83,040	94,129
	91,154	83,752	73,968	72,411	69,618	54,625	38,824	28,933
	141,549	134,697	126,824	135,146	143,378	135,158	122,674	124,011
	¥ 5,264	¥ 5,237	¥ 5,479	¥ 3,124	¥ 3,906	¥ 4,090	¥ 2,441	¥ 3,631
	4,123	3,770	3,958	4,368	4,829	4,856	5,372	5,423
	3,453	3,225	3,298	3,396	2,777	2,761	2,782	2,517
	5,232	5,864	7,293	1,309	23,521	12,144	3,311	7,931
	12,047	12,019	10,634	5,358	12,687	14,593	5,063	10,775
	(6,815)	(6,155)	(3,341)	(4,049)	10,834	(2,448)	(1,752)	(2,844)
	(3,355)	(5,085)	(6,354)	(7,419)	(13,071)	(8,964)	(10,456)	(7,953)
	17,198	15,318	14,596	13,718	19,812	9,326	6,018	(13,189)
	¥ 183.55	¥ 151.77	¥ 152.80	¥ 129.57	¥ 186.43	¥ 173.62	¥ 145.81	¥ 118.97
	58.00	46.00	34.00	23.00	17.00	14.00	12.00	13.00
	1,274.06	1,175.04	1,037.76	1,015.46	970.50	772.34	548.39	408.54
	68.9%	68.6%	67.8%	66.7%	67.7%	69.0%	68.7%	68.8%
	46.2	47.8	49.4	50.0	50.7	50.8	54.6	55.1
	22.7	20.8	18.3	16.7	17.0	18.2	14.1	13.7
	22.2	20.6	19.9	15.4	23.3	16.3	10.1	11.1
	13.7	11.8	12.0	9.6	14.4	13.7	12.3	10.3
	15.0	13.7	14.9	13.0	21.3	26.5	30.7	37.7
	15.6	14.5	12.6	11.4	11.1	12.8	9.7	9.3
	189.1	173.8	157.2	142.3	133.7	107.7	106.9	99.1

Management's Discussion and Analysis

Tsumura's Financial History

Favorable Growth for Kampo Products

Following NHI Listing

In 1976, 33 of Tsumura's pharmaceutical Kampo products were approved under the National Health Insurance (NHI) plan. Tsumura's Kampo product sales were only ¥1.87 billion in the fiscal year ended March 1977, but grew steadily starting in the following year. Three years later, in the fiscal year ended March 1980, Tsumura's Kampo product sales surged to ¥10 billion. In 1987, the Company had a total of 129 prescription Kampo products approved under the NHI plan. Later, clinical data was announced demonstrating the efficacy of TJ-9 (Shosaikoto), a Kampo medicine for colds, in treating chronic hepatitis. Consequently, Tsumura's sales of prescription Kampo products rose substantially to approximately ¥100 billion in the fiscal year ended March 1992. Of this amount, about one-third was sales of TJ-9 (Shosaikoto).

Adverse Reactions Problem Causes Sales to Stagnate

Prescription Kampo product sales continued to record favorable growth, but then news of an unexpected adverse reaction from treatment with TJ-9 (Shosaikoto) emerged.

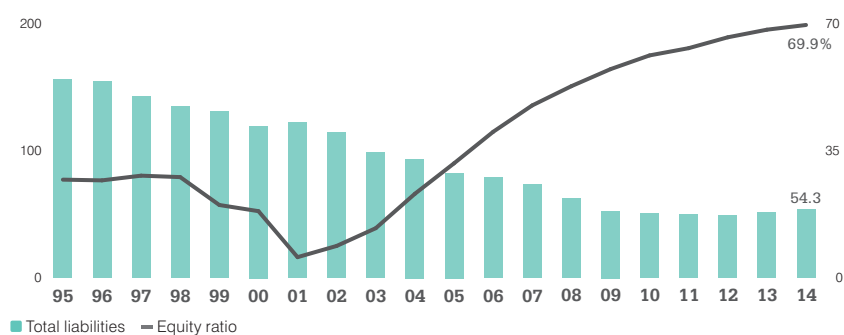
This news was followed by the announcement of a warning about using the product in 1991. Although the frequency of occurrence of interstitial pneumonia caused by treatment with TJ-9 (Shosaikoto) was low compared with Western drugs, the public's confidence was shaken because it was commonly believed that Kampo medicines did not have any adverse reactions. This news had a negative impact on the public's image of Kampo products and consequently sales slumped. Moreover, we pursued a business diversification strategy at that time, and many of those businesses began to produce red ink, resulting in deterioration in our financial position.

Specialization in Kampo Business

To overcome its business crisis, Tsumura changed its business policy drastically, shifting to one specializing in the development of the Kampo medicines business. Under the revised business policy, the Company focused its efforts on patiently promoting the popularization of Kampo medicine through actions aimed at disseminating a proper understanding and awareness of Kampo medicine among students at medical schools and universities, clinical physicians, and general consumers. Specifically,

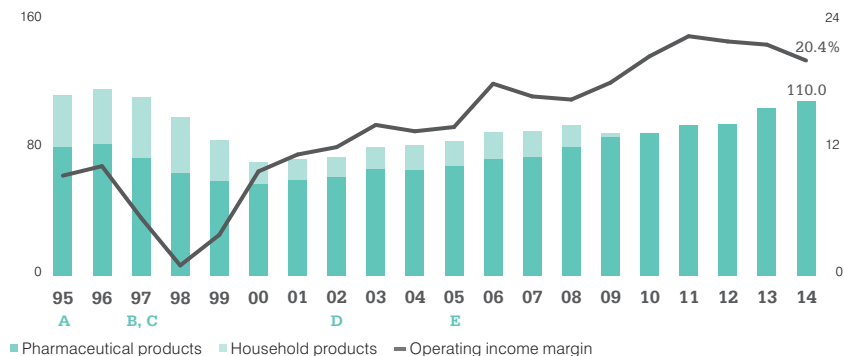
Total Liabilities / Equity Ratio

¥ billion / %



Net Sales / Operating Income Margin

¥ billion / %



- A In 1991, Interferon was indicated for the treatment of hepatitis C and a warning was issued about a possible adverse reaction (interstitial pneumonia) of TJ-9 (Shosaikoto). In 1994, the combined use of TJ-9 (Shosaikoto) and Interferon was prohibited.
- B First reported TJ-9 (Shosaikoto) related deaths
- C Extensive media coverage of possible adverse reactions of TJ-9 (Shosaikoto)
- D Education ministry introduces model core curriculum—Outline of Kampo drugs approved
- E Kampo education available at all 80 Japanese medical schools

the Company began activities to support Kampo medicine education at medical schools and universities, implemented Kampo medicine seminars for clinical physicians, and held public lectures on Kampo medicine for general consumers. As a result of these efforts, sales bottomed out in the fiscal year ended March 2000 and have continued to rebound since then—as has Tsumura's financial position. Moreover, in 2008, the Company divested its household products business in order to further specialize in its Kampo medicine business.

Tsumura's Business

Our principal business is the manufacture and sale of pharmaceutical products, including primarily prescription Kampo products covered under the NHI plan as well as OTC Kampo products. We also used to have a household products business that manufactured and marketed household products, mainly bath additives and hair-growth agents. However, with the sale of all of the shares of Tsumura Lifescience Co., Ltd., on August 29, 2008, we now focus only on pharmaceutical products.

Income Statement

Overview of Results

¥ in millions, except ratios

	2014	2013
Net sales	¥110,057	¥105,638
Gross profit	71,269	69,711
Gross profit margin	64.8%	66.0%
Operating income	¥ 22,461	¥ 23,124
Operating income margin	20.4%	21.9%
Net income	¥ 18,050	¥ 15,373

Net Sales

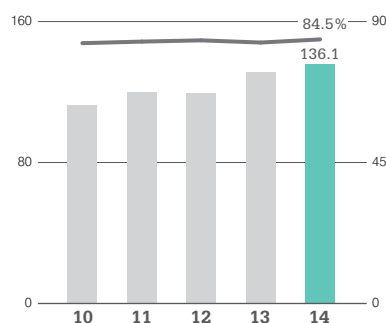
During the fiscal year under review, the business environment in the prescription Kampo product market remained difficult. There was no change in the Japanese government's policy of curtailing medical care expenses, as it implemented another revision of official drug prices in April 2014, among other measures.

Notwithstanding the arduous business climate, Tsumura's consolidated net sales climbed 4.2% from a year earlier, to ¥110,057 million. A solid increase in the sales of prescription Kampo products supported overall sales growth. Underpinned by the sales growth of the five drug fostering and evolution of Kampo program formulations and aided by the positive contribution from foreign exchange rate fluctuations to internal transaction differences, total sales of the Company's prescription Kampo product sales increased 3.2% year on year, to ¥102,680 million.

Underlying the firm growth in prescription Kampo product sales was Tsumura's steady progress with its drive to expand the Kampo medicine market. We have been concentrating on disseminating Kampo medicine and Kampo products information through reinforcement of our sales visits and consultation activities for physicians. In addition, we have also done so by proactively conducting Kampo medicine seminars, lectures, study groups, and medical institution information meetings, and study groups for physicians-in-training working at designated hospitals for clinical training. And we continued to build quality scientific evidence on the efficacy and safety of the five Kampo products featured in Tsumura's "drug fostering" program—TJ-100 (Daikenchuto), TJ-43 (Rikkunshito), TJ-54 (Yokukansan), TJ-107 (Goshajinkigan), and TJ-14 (Hangeshashinto). We announced research results at various academic conferences and published them in research papers. In addition,

Japanese Market Size for Prescription Kampo Products*

¥ billion / %



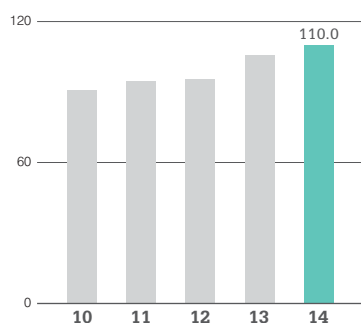
■ Overall market — Tsumura's share

* NHI Listed Price

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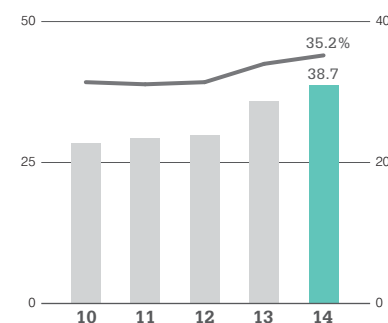
Net Sales

¥ billion



Cost of Sales / Cost of Sales Ratio

¥ billion / %



■ Cost of sales — Cost of sales ratio

as a result of our scientific evidence-based market efforts through our medical representatives, the reputation of our Kampo products is rising in various medical specialty fields. Reflecting this progress, sales of the five “drug fostering” program prescription Kampo products increased 6.9% from a year earlier, continuing to drive growth in overall prescription Kampo products.

Cost of Sales

Cost of sales rose 8.0% from last year, to ¥38,787 million. The increase can be attributed to a rise in the cost of the crude drugs used as raw materials for our prescription Kampo products for various reasons, including increased demand. In addition, there was a delayed impact on crude drug inventories of the sharp depreciation on the Japanese yen since the start of 2013 because of the Company's significant level of inventories. The cost of sales ratio increased 1.2 percentage points year on year, to 35.2%. Despite a positive contribution from the improvement in the manufacturing cost due to higher production volumes, the cost of sales ratio worsened because of the previously mentioned increased in raw material prices.

Selling, General and Administrative (SG&A) Expenses

Selling, general and administrative (SG&A) expenses increased 4.8%, to ¥48,808 million because of growth in, among others, sales-related and R&D expenses. Reflecting these cost increases, the SG&A expenses margin worsened 0.2 percentage point, to 44.3%.

Among major SG&A expenses, sales promotion expenses rose 6.3%, to ¥4,477 million, while sales rebate expenses edged up 2.8%, to ¥7,904 million, and salaries and allowances increased 1.8%, to ¥17,171 million.

In contrast, provision for employees' retirement and severance benefits contracted 8.4%, to ¥1,086 million.

Among other SG&A expenses, advertising cost climbed 9.0%, to ¥969 million, while R&D expenses jumped 21.3% from a year earlier, to ¥5,949 million. The higher R&D expenses can be attributed to the “drug fostering” program and intensified R&D efforts in the United States related to the development of TU-100 (Daikenchuto).

Major Expenses

¥ in millions	2014	2013
Personnel expenses	¥28,886	¥27,663
Sales promotion expenses	4,477	4,213
Advertising cost	969	889
R&D expenses	5,949	4,904

Operating Income

Operating income decreased 2.9%, to ¥22,461 million. The operating income margin declined 1.5 percentage points, to 20.4%.

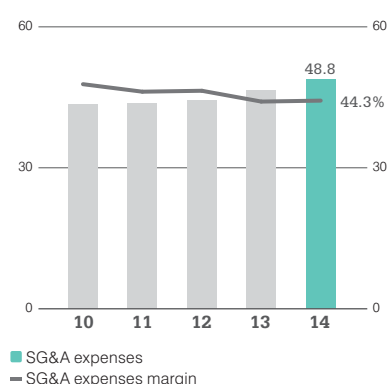
Net Income

Consolidated net income rose 17.4% year on year, to ¥18,050 million. Profit growth can be attributed to a ¥4,416 million gain on sales of investment securities and a year-on-year increase of ¥290 million from foreign exchange gain due to the weaker yen. The lack of the one-time impairment losses on fixed assets recorded in the previous fiscal year due to the disposal of distribution facilities also contributed to profit growth. As a result, net income advanced ¥2,677 million year on year.

Net income per share increased to ¥255.94 per share, compared with ¥217.98 per share a year earlier.

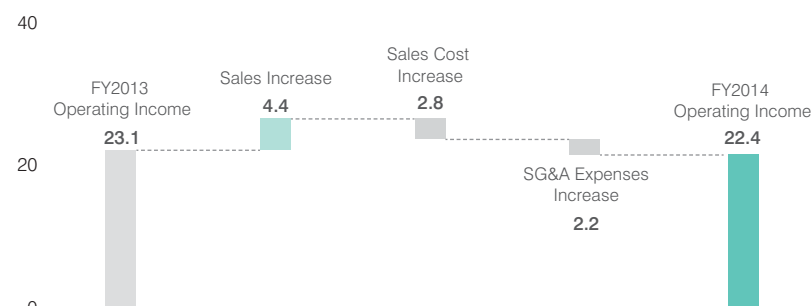
SG&A Expenses / SG&A Expenses Margin

¥ billion / %



Factors in Increase / Decrease of Operating Income

¥ billion



Liquidity and Capital Resources

Cash Flows

Cash Flows

¥ in millions

	2014	2013
Cash flows from operating activities	¥5,908	¥12,011
Cash flows from investing activities	(1,694)	(8,022)
Cash flows from financing activities	(4,575)	(4,275)

Net cash provided by operating activities amounted to ¥5,908 million during the fiscal year, decreasing ¥6,102 million year on year. Among cash inflows, there was an increase in income before income taxes and minority interests and a decrease in receivables. However, cash outflows expanded more based on an increase in inventories and expenses for strategic procurement of certain raw material crude drugs booked in others, net.

Net cash used in investing activities amounted to ¥1,694 million, decreasing ¥6,327 million from a year earlier. Cash inflows increased because of proceeds from sales and redemption of investment securities, while cash outflows declined because of decreased expenditures on purchase of property, plant and equipment and investment securities.

Net cash used in financing activities amounted to ¥4,575 million, increasing ¥299 million from last year. The increase can be attributed to growth in cash dividends.

As a result of the above activities, the balance of cash and cash equivalents at the end of the fiscal year was ¥14,418 million, an increase of ¥656 million from the beginning of the fiscal year.

Balance Sheet

Balance Sheet Data

¥ in millions

	2014	2013
Total assets	¥187,623	¥170,466
Total liabilities	54,305	51,929
Interest-bearing debt	22,088	22,059
Total net assets	133,318	118,537

Assets

Compared with the end of the previous fiscal year, current assets grew ¥14,164 million, to ¥108,692 million. Among the categories posting growth were trade notes and accounts receivable, raw materials and supplies because of the increase in the prices of certain raw material crude drugs and the impact of the weaker yen, work in process, and merchandise and finished goods.

Fixed assets increased ¥2,992 million, to ¥78,931 million. Although investment securities contracted, fixed assets rose because of growth in plant and equipment arising from the expansion of manufacturing facilities at the Ibaraki Plant, the Shizuoka Plant, and SHANGHAI TSUMURA PHARMACEUTICALS CO., LTD.

Overall, total assets amounted to ¥187,623 million, rising ¥17,156 million from the previous fiscal year.

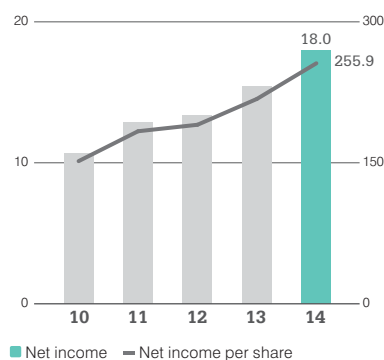
Liabilities

Current liabilities increased ¥2,698 million year on year, to ¥45,179 million. Although accounts payable—other declined, income taxes payable increased, resulting in an overall increase. In contrast, long-term liabilities decreased ¥322 million, to ¥9,126 million, mainly because of a reduction in deferred tax liabilities. Interest-bearing debt, however, edged up to ¥22,088 million, increasing ¥28 million from last year.

Consequently, total liabilities at the end of the fiscal year increased ¥2,375 million from the prior year, to ¥54,305 million.

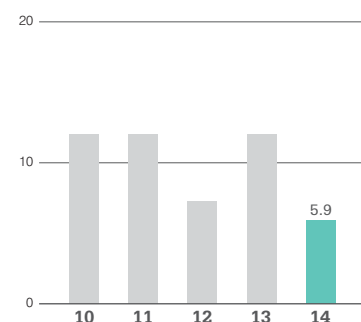
Net Income / Net Income per Share

¥ billion / ¥



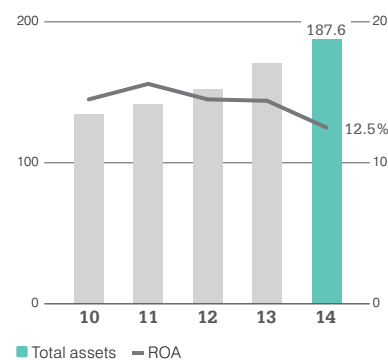
Cash Flows from Operating Activities

¥ billion



Total Assets / ROA

¥ billion / %



Net Assets

At fiscal year-end, net assets amounted to ¥133,318 million, increasing ¥14,780 million from a year earlier. The increase can be attributed to the growth in retained earnings and in translation adjustments.

Financial Policy

To increase profitability, the Company is working to build free cash flow and optimize its capital structure. Seeking to enhance corporate value, Tsumura's management has positioned ROE as an important performance indicator. In the fiscal year under review, despite shareholders' equity expanding because of growth in retained earnings related to the increase in net income, ROE rose 0.4 percentage point from a year earlier, to 14.5%. ROA declined 1.8 percentage points, to 12.5%. The equity ratio improved 1.3 percentage points year on year, to 69.9%, while the debt-to-equity ratio declined to 0.41 times from 0.44 times the previous year. Tsumura is committed to continuing its efforts to implement thoroughly efficient operations and strengthen its financial structure.

Currently, the Company is progressing with manufacturing cost structure reforms, planning to allocate the cash earned from operating activities to capital and other investment in growth, such as the improvement of the productivity of existing facilities and the introduction of new manufacturing technologies.

At the same time, Tsumura places great importance on returning profits to shareholders. For that reason, the Company's policy is to achieve stable dividend payouts after taking into consideration capital investment, consolidated performance, and the dividend payout ratio. For the fiscal year under review, Tsumura increased total annual dividends by ¥2.0 per share, to ¥64.0 per share, resulting

in the dividend payout ratio declining 3.4 percentage points, to 25.0%.

Financial Policy and Dividend Policy

%	2014	2013
ROE	14.5%	14.1%
ROA	12.5	14.3
Equity ratio	69.9	68.6
Debt-to-equity ratio (times)	0.41	0.44

Risk Factors

In the following discussion of risk factors, major risks related to the Group's businesses that may exert a significant influence on investors' judgment are outlined. From the standpoint of proactive information disclosure, we have included references to matters that do not necessarily constitute risk factors but we believe are important for investors to consider. The Tsumura Group will strive to avoid the materialization of such risks; however, should such risks materialize, we will endeavor to minimize their impact.

This discussion includes issues that are not yet pertinent to the Group's performance. However, they have been included as management has deemed them important as of 27 June, 2013.

(1) Medical system

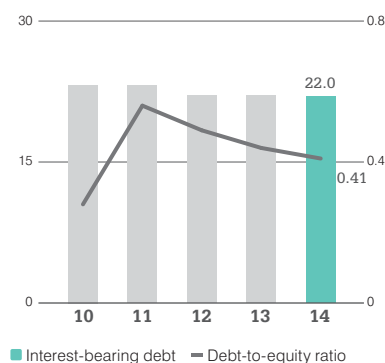
In the pharmaceutical industry, changes to medical care systems exert a major influence on the market environment. Depending on the direction of change, a negative effect on the industry as a whole and on the Tsumura Group could result.

(2) Competition

In Japan, we have long maintained a dominant position in the field of prescription Kampo products, which is the

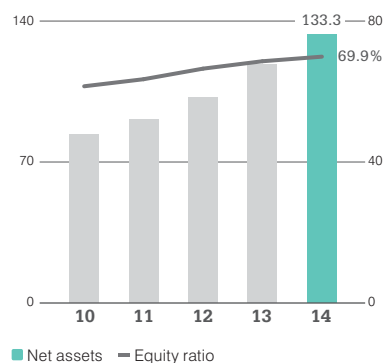
Interest-Bearing Debt / Debt-to-Equity Ratio

¥ billion / Times



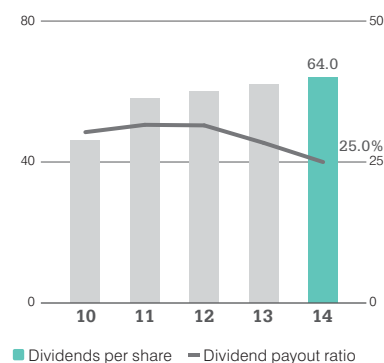
Net Assets / Equity Ratio

¥ billion / %



Dividends per Share / Dividend Payout Ratio

¥ / %



mainstay of the Group. However, if a major domestic or foreign pharmaceuticals company entered the Kampo medicines market, competition would intensify further, and the Group's performance could suffer.

(3) Product supply

Approximately 80% of the crude drug medicinal plants that constitute the main ingredients of Tsumura's Kampo formulations are imported from China, and some processes in the production of Kampo products are commissioned to subsidiaries situated in China. Because most of the medicinal plants grow wild, we are researching the cultivation of major medicinal plants for the future. However, in the event of unforeseeable changes in legal regulations or political or economic conditions, it could become difficult to secure or import sufficient quantities. In addition, bad weather, natural disasters, or wars could destabilize social conditions, creating instability in the circulation of demand of the raw materials and supply of them procured domestically and internationally for the manufacture of products, which could have a negative impact on the supply of products due to hikes in the market prices of the raw materials or scarcity of their supply.

Likewise, while we have incorporated earthquake-resistant features in construction and conduct regular inspections of equipment and facilities within Japan, we cannot completely guarantee that the functioning of our facilities will not be hampered or lost in the event of a massive earthquake, fire, power outage, or other disaster. The Group's social standing or performance could be negatively affected should the supply of products be interrupted or delayed due to the above.

(4) Product safety and adverse reactions

In the manufacturing of the Group's products, we strictly adhere to the quality control standards of the countries in which we operate and our own original standard for crude drugs. However, we cannot completely guarantee that there will not be a defect or safety problem, including undetected pesticide residue on a medicinal plant used in a Kampo product. In addition, should consumers experience unexpected adverse reactions from a pharmaceutical product marketed by the Tsumura Group, the existing methods of use may be restricted, and a loss of confidence in the Group and its pharmaceutical products may result in a drop in the dispensation of our medicines or in

patients' refusal to take them. The Tsumura Group's performance may suffer if a situation such as the above results in a decline in sales volume, demand for large amounts of damage compensation, or a large-scale recall, among other possibilities.

(5) R&D

In the interest of future growth and better corporate performance, the Tsumura Group conducts R&D activities related to new products and new technologies both in Japan and abroad. However, we cannot guarantee that all of these activities will be successful. The Group's performance could suffer if for some reason R&D activities were canceled or delayed or if costs increased significantly.

(6) International business

The Tsumura Group engages in the manufacture and sale of pharmaceuticals in China, South Korea, and other foreign countries. Because of this involvement in international business, it is possible for the Group to be negatively affected by unforeseeable changes in legal regulations or in political, economic, or other conditions.

(7) Financial condition

The Group's performance and financial condition could be negatively affected by such conditions as sharp increases in declining share prices or increased retirement liabilities arising from a drop in the discount rate.

(8) Intellectual property

We cannot guarantee the full protection of the intellectual property owned by the Group in relation to Kampo products, and others. The Group's performance may be negatively affected if there were leakage of such information, leading to a decline in competitiveness.

(9) Exchange rate fluctuations

The Group imports from China most of the crude drugs used in the Kampo products that it markets. Therefore, sharp movements in exchange rates could impact negatively on the Group's business results and financial position.

FINANCIAL SECTION

Consolidated Balance Sheets

TSUMURA & CO. and consolidated subsidiaries
March 31, 2014 and 2013

	¥ in millions		US\$ in thousands (Note 2)
ASSETS	2014	2013	2014
Current assets:			
Cash and time deposits (Notes 4 and 13)	¥ 14,445	¥ 13,793	\$ 140,357
Trade notes and accounts receivable (Note 4)	39,553	37,199	384,310
Less allowance for doubtful receivables	(3)	(3)	(37)
Inventories (Note 5)	43,424	35,565	421,921
Deferred tax assets (Note 8)	1,654	1,123	16,073
Other current assets	9,618	6,850	93,457
Total current assets	108,692	94,527	1,056,082
Investments and other assets:			
Investments in non-consolidated subsidiaries and affiliates (Note 4)	2,349	2,249	22,833
Investment securities (Notes 3 and 4)	15,842	19,741	153,933
Deferred tax assets (Note 8)	26	35	258
Other assets	3,357	3,023	32,623
Less allowance for doubtful accounts	(4)	(4)	(43)
Total investments and other assets	21,572	25,045	209,604
Property, plant and equipment, at cost:			
Land (Note 6)	9,897	9,897	96,163
Buildings and structures	57,088	47,944	554,692
Machinery and equipment	39,653	34,955	385,289
Tools, furniture and fixtures	8,281	7,387	80,461
Construction in progress	3,224	7,407	31,328
Others	225	206	2,194
Less accumulated depreciation	(61,222)	(57,142)	(594,859)
Property, plant and equipment, net	57,148	50,657	555,269
Intangible assets, net of accumulated amortization	210	235	2,049
Total assets	¥187,623	¥170,466	\$1,823,006

	¥ in millions		US\$ in thousands (Note 2)
LIABILITIES AND NET ASSETS	2014	2013	2014
Current liabilities:			
Short-term bank loans (Notes 4 and 7)	¥ 21,957	¥ 21,957	\$ 213,340
Current portion of long-term debt (Note 7)	33	26	321
Trade notes and accounts payable (Note 4)	3,210	2,954	31,190
Income taxes payable (Notes 4 and 8)	5,890	4,222	57,236
Accounts payable—other (Note 4)	6,357	8,649	61,773
Allowance for sales returns	8	9	80
Other current liabilities	7,722	4,662	75,033
Total current liabilities	45,179	42,480	438,976
Long-term liabilities:			
Long-term debt, less current portion (Note 7)	98	76	954
Deferred tax liabilities other than unrealized revaluation gain on land (Note 8)	66	997	644
Deferred tax liability—unrealized revaluation gain on land (Note 6)	1,559	1,559	15,149
Accrued employees' retirement and severance benefits (Note 9)	—	2,055	—
Net defined benefit liability (Note 9)	2,341	—	22,749
Other long-term liabilities	5,061	4,759	49,174
Total long-term liabilities	9,126	9,448	88,671
Net assets: (Note 10)			
Shareholders' equity:			
Common stock	19,487	19,487	189,349
Authorized—250,000,000 shares in 2014 and 2013			
Issued—70,771,662 shares in 2014 and 2013			
Capital surplus	1,940	1,940	18,855
Retained earnings	103,934	90,397	1,009,856
Treasury stock, at cost	(388)	(385)	(3,772)
Total shareholders' equity	124,974	111,440	1,214,289
Accumulated other comprehensive income:			
Unrealized holding gain on other securities, net of taxes	1,861	3,394	18,085
Deferred gain on hedges, net of taxes	552	987	5,370
Unrealized revaluation gain on land, net of taxes (Note 6)	1,984	1,984	19,281
Translation adjustments	2,259	(812)	21,957
Remeasurements of defined benefit plans	(445)	—	(4,331)
Total accumulated other comprehensive income	6,212	5,554	60,362
Minority interests in consolidated subsidiaries:	2,131	1,542	20,705
Total net assets	133,318	118,537	1,295,357
Total liabilities and net assets	¥187,623	¥170,466	\$1,823,006

See notes to consolidated financial statements.

FINANCIAL SECTION

Consolidated Statements of Income

TSUMURA & CO. and consolidated subsidiaries
For the years ended March 31, 2014 and 2013

	¥ in millions		US\$ in thousands (Note 2)
	2014	2013	2014
Net sales	¥110,057	¥105,638	\$1,069,352
Cost of sales (Note 5)	38,788	35,928	376,881
Gross profit before allowance for sales returns	71,269	69,709	692,471
Reversal of allowance for sales returns	0	1	7
Gross profit	71,269	69,711	692,479
Selling, general and administrative expenses (Note 12)	48,808	46,586	474,235
Operating income	22,461	23,124	218,243
Other income (expenses):			
Interest and dividends received	383	365	3,729
Interest expenses	(186)	(216)	(1,811)
Equity in income of affiliates	2	15	22
Foreign exchange gain	962	672	9,356
Gain on sales of property, plant and equipment	2	1	25
Loss on sales and disposition of property, plant and equipment	(267)	(142)	(2,597)
Impairment losses (Note 18)	–	(184)	–
Gain on sales of investment securities (Note 3)	4,416	2	42,910
Gain on sales of investments in subsidiaries and affiliates	–	75	–
Other, net	342	348	3,325
Total other income (expenses)	5,656	937	54,961
Income before income taxes and minority interests	28,118	24,062	273,205
Income taxes (Note 8):			
Current	9,937	8,761	96,555
Deferred	(27)	(174)	(262)
Subtotal	9,910	8,587	96,292
Net income before minority interests	18,207	15,475	176,913
Minority interests	(157)	(102)	(1,527)
Net income	¥ 18,050	¥ 15,373	\$ 175,385

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Income

TSUMURA & CO. and consolidated subsidiaries
For the years ended March 31, 2014 and 2013

	¥ in millions		US\$ in thousands (Note 2)
	2014	2013	2014
Net income before minority interests	¥18,207	¥15,475	\$176,913
Other comprehensive income (Note 16):			
Unrealized holding gain (loss) on other securities, net of taxes	(1,533)	3,458	(14,896)
Deferred gain (loss) on hedges, net of taxes	(434)	600	(4,226)
Translation adjustments	3,447	983	33,497
Share of other comprehensive income of affiliates accounted for using equity method	94	38	921
Total other comprehensive income	1,574	5,080	15,296
Comprehensive income	¥19,782	¥20,555	\$192,209
Total comprehensive income attributable to:			
Interests of the parent	¥19,154	¥20,307	\$186,111
Minority interests	627	248	6,097

See notes to consolidated financial statements.

Consolidated Statements of Changes in Net Assets

TSUMURA & CO. and consolidated subsidiaries
For the years ended March 31, 2014 and 2013

	Number of shares of common stock	Shareholders' equity				
		Common stock	Capital surplus	Retained earnings	Treasury stock	Total shareholders' equity
Balance at April 1, 2013	70,771,662	¥19,487	¥1,940	¥ 90,397	¥(385)	¥111,440
Cash dividends paid	—	—	—	(4,513)	—	(4,513)
Net income	—	—	—	18,050	—	18,050
Purchase of treasury stock	—	—	—	—	(2)	(2)
Net changes in items other than those in shareholders' equity	—	—	—	—	—	—
Total changes during the year	—	—	—	13,537	(2)	13,534
Balance at March 31, 2014	70,771,662	¥19,487	¥1,940	¥103,934	¥(388)	¥124,974

	Accumulated other comprehensive income							¥ in millions
	Unrealized holding gain on other securities, net of taxes	Deferred gain on hedges, net of taxes	Unrealized revaluation gain on land, net of taxes (Note 6)	Translation adjustments	Remeasurements of defined benefit plans	Total accumulated other comprehensive income	Minority interests in consolidated subsidiaries	Total net assets
Balance at April 1, 2013	¥ 3,394	¥ 987	¥1,984	¥ (812)	¥ –	¥5,554	¥1,542	¥118,537
Cash dividends paid	–	–	–	–	–	–	–	(4,513)
Net income	–	–	–	–	–	–	–	18,050
Purchase of treasury stock	–	–	–	–	–	–	–	(2)
Net changes in items other than those in shareholders' equity	(1,533)	(434)	–	3,072	(445)	658	588	1,246
Total changes during the year	(1,533)	(434)	–	3,072	(445)	658	588	14,780
Balance at March 31, 2014	¥1,861	¥ 552	¥1,984	¥2,259	¥(445)	¥6,212	¥2,131	¥133,318

	Number of shares of common stock	Shareholders' equity				
		Common stock	Capital surplus	Retained earnings	Treasury stock	Total shareholders' equity
Balance at April 1, 2013	70,771,662	\$189,349	\$18,855	\$ 878,327	\$(3,748)	\$1,082,783
Cash dividends paid	—	—	—	(43,856)	—	(43,856)
Net income	—	—	—	175,385	—	175,385
Purchase of treasury stock	—	—	—	—	(24)	(24)
Net changes in items other than those in shareholders' equity	—	—	—	—	—	—
Total changes during the year	—	—	—	131,529	(24)	131,505
Balance at March 31, 2014	70,771,662	\$189,349	\$18,855	\$1,009,856	\$(3,772)	\$1,214,289

	US\$ in thousands (Note 2)							
	Accumulated other comprehensive income							
	Unrealized holding gain on other securities, net of taxes	Deferred gain on hedges, net of taxes	Unrealized revaluation gain on land, net of taxes (Note 6)	Translation adjustments	Remeasurements of defined benefit plans	Total accumulated other comprehensive income	Minority interests in consolidated subsidiaries	Total net assets
Balance at April 1, 2013	\$ 32,981	\$ 9,596	\$19,281	\$ (7,891)	\$ –	\$53,968	\$14,989	\$1,151,741
Cash dividends paid	–	–	–	–	–	–	–	(43,856)
Net income	–	–	–	–	–	–	–	175,385
Purchase of treasury stock	–	–	–	–	–	–	–	(24)
Net changes in items other than those in shareholders' equity	(14,896)	(4,226)	–	29,848	(4,331)	6,394	5,716	12,110
Total changes during the year	(14,896)	(4,226)	–	29,848	(4,331)	6,394	5,716	143,616
Balance at March 31, 2014	\$ 18,085	\$ 5,370	\$19,281	\$21,957	\$(4,331)	\$60,362	\$20,705	\$1,295,357

See notes to consolidated financial statements.

FINANCIAL SECTION

	Number of shares of common stock	¥ in millions				
		Shareholders' equity				
		Common stock	Capital surplus	Retained earnings	Treasury stock	Total shareholders' equity
Balance at April 1, 2012	70,771,662	¥19,487	¥1,940	¥79,255	¥(384)	¥100,300
Cash dividends paid	—	—	—	(4,231)	—	(4,231)
Net income	—	—	—	15,373	—	15,373
Purchase of treasury stock	—	—	—	—	(1)	(1)
Net changes in items other than those in shareholders' equity	—	—	—	—	—	—
Total changes during the year	—	—	—	11,141	(1)	11,140
Balance at March 31, 2013	70,771,662	¥19,487	¥1,940	¥90,397	¥(385)	¥111,440

	¥ in millions						
	Accumulated other comprehensive income						
	Unrealized holding gain (loss) on other securities, net of taxes	Deferred gain on hedges, net of taxes	Unrealized revaluation gain on land, net of taxes (Note 6)	Translation adjustments	Remeasurements of defined benefit plans	Total accumulated other comprehensive income	Minority interests in consolidated subsidiaries
Balance at April 1, 2012	¥ (63)	¥387	¥1,984	¥(1,687)	¥—	¥ 619	¥1,321
Cash dividends paid	—	—	—	—	—	—	—
Net income	—	—	—	—	—	—	—
Purchase of treasury stock	—	—	—	—	—	—	—
Net changes in items other than those in shareholders' equity	3,458	600	—	875	—	4,934	221
Total changes during the year	3,458	600	—	875	—	4,934	221
Balance at March 31, 2013	¥3,394	¥987	¥1,984	¥ (812)	¥—	¥5,554	¥1,542

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

TSUMURA & CO. and consolidated subsidiaries
For the years ended March 31, 2014 and 2013

	¥ in millions		US\$ in thousands (Note 2)
	2014	2013	2014
Cash flows from operating activities:			
Income before income taxes and minority interests	¥28,118	¥24,062	\$273,205
Adjustments to reconcile income before income taxes and minority interests to net cash provided by operating activities:			
Depreciation	4,871	4,049	47,328
Impairment losses (Note 18)	–	184	–
Interest and dividends received	(383)	(365)	(3,729)
Interest expenses	186	216	1,811
Equity in (income) of affiliates	(2)	(15)	(22)
Loss on sales and disposition of property, plant and equipment	199	124	1,939
(Gain) on sales of investment securities	(4,416)	(2)	(42,910)
(Gain) on sales of investments in subsidiaries and affiliates	–	(75)	–
(Increase) in receivables	(2,291)	(2,626)	(22,268)
(Increase) in inventories	(5,728)	(4,262)	(55,657)
Increase (decrease) in allowance for doubtful receivables	0	(29)	4
(Decrease) in payables and accrued expenses	(90)	(426)	(877)
Increase in accrued employees' retirement and severance benefits	–	122	–
(Decrease) in net defined benefit liability	(407)	–	(3,956)
Others, net	(6,086)	847	(59,135)
Subtotal	13,969	21,805	135,732
Interest and dividends received	411	385	4,003
Interest paid	(184)	(216)	(1,788)
Income taxes paid	(8,288)	(9,963)	(80,534)
Net cash provided by operating activities	5,908	12,011	57,412
Cash flows from investing activities:			
Purchase of property, plant and equipment	(7,669)	(7,991)	(74,520)
Proceeds from sales of property, plant and equipment	29	4	284
Purchase of intangible assets	(21)	(60)	(212)
Purchase of investment securities	(9)	(209)	(95)
Proceeds from sales and redemption of investment securities	5,916	4	57,482
Purchase of investments in subsidiaries and affiliates	–	(100)	–
Payments of loans receivable	(10)	(249)	(98)
Collection of loans receivable	9	10	88
Deposits of time deposits with maturity of more than three months	(44)	(43)	(427)
Refunds of time deposits with maturity of more than three months	48	45	466
Others, net	58	568	568
Net cash used in investing activities	(1,694)	(8,022)	(16,464)
Cash flows from financing activities:			
Repayments of long-term debt	(30)	(29)	(297)
Purchase of treasury stock	(2)	(1)	(24)
Cash dividends	(4,515)	(4,229)	(43,874)
Cash dividends paid to minority shareholders	(26)	(14)	(258)
Net cash used in financing activities	(4,575)	(4,275)	(44,454)
Effect of exchange rate changes on cash and cash equivalents	1,016	142	9,880
Net increase (decrease) in cash and cash equivalents	656	(144)	6,374
Cash and cash equivalents at beginning of year	13,762	13,906	133,720
Cash and cash equivalents at end of year (Note 13)	¥14,418	¥13,762	\$140,094

See notes to consolidated financial statements.

Notes to the Consolidated Financial Statements

TSUMURA & CO. and consolidated subsidiaries
For the year ended March 31, 2014

1 Summary of Significant Accounting Policies

(a) Basis of presentation

The accompanying consolidated financial statements of TSUMURA & CO. (the "Company") and its consolidated subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the Financial Instruments and Exchange Act of Japan (the "FIEA").

As permitted by the FIEA, amounts of less than one million yen have been omitted. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and in U.S. dollars) do not necessarily agree with the sums of the individual amounts.

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation.

(b) Principles of consolidation and accounting for investments in unconsolidated subsidiaries and affiliates

The accompanying consolidated financial statements include the accounts of the Company and any significant companies controlled directly or indirectly by the Company. Companies over which the Company exercises significant influence in terms of their operating and financial policies have been accounted for by the equity method.

The consolidated financial statements include the accounts of the Company and its five significant subsidiaries for the years ended March 31, 2014 and 2013. All significant inter-company balances and transactions have been eliminated in consolidation.

The equity method is applied to investments in significant affiliates in accordance with the provisions of the Accounting Standard for Consolidated Financial Statements.

Investments in non-consolidated subsidiaries and other affiliates are stated at cost. If the equity method had been applied to the investments in these companies, there would have been no material effect in the accompanying consolidated financial statements.

(c) Accounting period

The accounting period of the Company begins on April 1 and ends on March 31 of the following year. The three overseas consolidated subsidiaries have fiscal years ending on December 31. The necessary adjustments for significant transactions, if any, during the intervening period are made on consolidation.

(d) Translation of foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into yen at the rates in effect at the balance sheet date and the accounts of the overseas consolidated subsidiaries, etc., except for the components of shareholders' equity, which are translated into yen at the rates of exchange in effect at the balance sheet date. Foreign exchange gains and losses are credited or charged to operations and translation differences are included in net assets.

(e) Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows consist of cash on hand, demand deposits and liquid short-term investments with a maturity of three months or less from acquisition date.

(f) Marketable securities and investment securities

Trading securities are carried at market value and held-to-maturity securities are amortized or accumulated to face value. Money in trust with a market value is carried at market value.

Other securities with determinable market value are carried at market value with any changes in unrealized holding gain or loss in net assets. Other securities without determinable market value are stated at cost determined principally by the moving average method. The cost of other securities sold is principally computed based on the moving average method. The Company and its consolidated subsidiaries do not have any trading securities and held-to-maturity securities.

(g) Inventories

Inventories of the Company and its consolidated subsidiaries are mainly stated at cost determined by the average cost method of reducing book value when the contribution of inventories to profitability declines.

(h) Property, plant and equipment (except for leased assets)

Property, plant and equipment are stated at cost and depreciation of property, plant and equipment is computed by the straight-line method.

The estimated useful lives of the major depreciable assets are as follows:

Buildings and structures	3 to 65 years
Machinery and equipment	3 to 8 years

(i) Intangible assets (except for leased assets)

Intangible assets are amortized by the straight-line method. Cost of software purchased for internal use is amortized by the straight-line method over five years, the useful life applicable to commercially available software.

(j) Allowance for doubtful receivables

The Company and its consolidated subsidiaries provide allowances for losses on bad debts at the amounts estimated specifically on each doubtful receivable and the amounts calculated based on past experience for receivables other than specific doubtful receivables.

(k) Allowance for sales returns

Allowance for sales returns is provided for estimated losses on sales returns subsequent to the balance sheet date.

(l) Employees' retirement and severance benefits

The straight-line method is used as the method of attributing expected benefits to the current period in calculating retirement and severance benefit obligations.

Actuarial gains and losses and prior service costs are amortized using the straight-line method over 10 years, which is within the estimated average of remaining service years of employees.

The Company's consolidated subsidiaries use the simplified method in calculating net defined benefit liability and retirement benefit expenses. Under this method, the severance payment amount to be required at the year-end for voluntary termination is deemed as retirement and severance benefit obligations.

(m) Leased assets

Leased assets under finance lease transactions that do not transfer ownership to the lessee are depreciated under the straight-line method over the lease term with no residual value.

Among finance lease transactions that do not transfer ownership to the lessee, those lease transactions that commenced on or before March 31, 2008, are accounted for in a similar manner as operating lease transactions in accordance with generally accepted accounting standards.

(n) Income taxes

Deferred tax assets and liabilities are determined based on the differences between financial reporting and the tax bases of the assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

(o) Accounting for consumption taxes

Transactions subject to consumption taxes are recorded at amounts exclusive of consumption taxes. Consumption taxes paid by the Company and its consolidated subsidiaries on the purchases of goods and services that are not deductible under the Consumption Tax Law of Japan are expensed as incurred.

(p) Consolidated taxation system

The Company has applied the consolidated taxation system from the year ended March 31, 2014.

(q) Reclassifications

Certain prior year amounts have been reclassified to conform to the 2014 presentation. These changes had no impact on previously reported results of operations or net assets.

(r) Changes in accounting policies

From the year ended March 31, 2014, the Company has applied the "Accounting Standard for Retirement Benefits" (Accounting Standards Board of Japan ("ASBJ") Statement No. 26, May 17,

2012) and the "Guidance on Accounting Standard for Retirement Benefits" (ASBJ Guidance No. 25, May 17, 2012) (excluding Article 35 of the standard and Article 67 of the guidance). Under the new standard, the difference between retirement and severance benefit obligations and plan assets is recorded as net defined benefit liability, and unrecognized actuarial gains and losses and unrecognized prior service costs are also recorded in net defined benefit liability.

With regards to the application of the standard and the guidance, the effect of these changes is included in remeasurements of defined benefit plans in accumulated other comprehensive income as of March 31, 2014 in accordance with the transitional treatment in Article 37 of the standard.

As a result, net defined benefit liability of ¥2,341 million (U.S.\$22,749 thousand) was recorded, and accumulated other comprehensive income decreased by ¥445 million (U.S.\$4,331 thousand) as of March 31, 2014.

The effect of the accounting change on net assets per share is disclosed in Note 11: Amounts per Share.

(s) Accounting standards issued but not yet applied

On May 17, 2012, the ASBJ issued "Accounting Standard for Retirement Benefits" (ASBJ Statement No. 26) and "Guidance on Accounting Standard for Retirement Benefits" (ASBJ Guidance No. 25), which replaced the Accounting Standard for Retirement Benefits that had been issued by the Business Accounting Council in 1998 with an effective date of April 1, 2000 and the other related practical guidance, being followed by partial amendments from time to time through 2009.

The accounting standard for retirement benefits has been revised from the viewpoint of improvements to financial reporting and international convergence, mainly focusing on how unrecognized actuarial gains and losses and prior service costs should be accounted for, how retirement and severance benefit obligations and service costs should be determined, and the enhancement of disclosures.

The Company will adopt this standard and the guidance from the beginning of year ending March 31, 2015, with regard to the revisions relating to determination of retirement and severance benefit obligations and service costs.

As a result, the Company expects its operating income and income before income taxes and minority interests to decrease by ¥61 million (U.S.\$598 thousand), respectively, for the year ending March 31, 2015.

2 Basis of Translation

The consolidated financial statements presented herein are expressed in yen and, solely for the convenience of the reader, have been translated into U.S. dollars at ¥102.92=US\$1.00, the approximate exchange rate prevailing on the Tokyo Foreign

Exchange Market on March 31, 2014. This translation should not be construed as a representation that the amounts shown could have been, or could in the future be, converted into U.S. dollars at that or any other rate.

3 Investment Securities

The cost and related aggregate market values of securities, other than those held for trading and held-to-maturity purposes, with a readily available market value at March 31, 2014 and 2013, are summarized as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Cost	¥12,958	¥14,448	\$125,906
Market value	15,744	19,642	152,974
Total unrealized gain	3,674	5,870	35,705
Total unrealized loss	(888)	(676)	(8,637)

Securities as of March 31, 2014 and 2013 that are excluded from the above table are summarized at their book values as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Non-current assets:			
Unlisted stocks other than those on the over-the-counter market	¥98	¥98	\$959

Securities, other than those held for trading and held-to-maturity purposes, which were sold during the years ended March 31, 2014, and 2013, are summarized as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Proceeds received	¥4,916	¥4	\$47,765
Total gain	4,416	2	42,910
Total loss	—	—	—

The Company recognized impairment losses on all securities whose market value had declined by 50% or more of book value and on some securities whose market value had declined by 30% or more of book value. Impairment losses were, if any, recognized

at the amount of the difference between book value and market value. No impairment losses on securities were recognized for the years ended March 31, 2014 and 2013.

4 Financial Instruments

The Company and its consolidated subsidiaries finance short-term operating capital through bank loans, although capital investments for the pharmaceutical production and selling business are financed mainly by their own funds. Temporary excess funds are operated by highly rated financial institutions. Derivative transactions are only utilized to hedge the following risks, and it is our policy not to enter into derivative transactions for speculative purposes.

Operating receivables such as trade notes and accounts receivable are exposed to credit risk. The Company and its consolidated subsidiaries manage the due date and balance for each customer following internal rules and asking for deposits depending on the customer's credit conditions.

Investment securities mainly consist of securities of counterparties and are exposed to market fluctuation risk. The fair value of the investment securities is regularly reported to the responsible board of directors.

Operating payables such as trade notes and accounts payable are due within one year. Some of the operating payables relating to imports of raw materials are denominated in foreign currencies and are exposed to foreign currency fluctuation risk. The Company and its consolidated subsidiaries utilize foreign currency forward contracts to hedge the risk.

Short-term bank loans are used to finance operating capital and are exposed to interest rate fluctuation risk.

Accounts payable—other and Income taxes payable are each due within one year.

The Company and its consolidated subsidiaries utilize derivative financial instruments to hedge against such risks, such as foreign exchange forward contracts to hedge their foreign currency risk. Please refer to Note 15: Derivatives for information on hedge accounting.

Implementation and management of derivative transactions are based on internal rules. The Company and its consolidated subsidiaries only enter into derivative transactions with highly rated financial institutions to mitigate credit risk.

Operating payables and loans are exposed to liquidity risk. The Company and its consolidated subsidiaries manage the risk by preparing the cash management plans monthly.

The contract amount and other information regarding derivative transactions described in Note 15: Derivatives does not indicate market risk related to derivative transactions.

Carrying value on the consolidated balance sheets, fair values, and differences of financial instruments as of March 31, 2014 and 2013, are as follows:

¥ in millions			
2014			
	Carrying value reported in the balance sheet	Fair value	Difference
Cash and time deposits	¥14,445	¥14,445	¥—
Trade notes and accounts receivable	39,553	39,553	—
Investment securities:			
Other securities	15,744	15,744	—
Total	¥69,742	¥69,742	¥—
Trade notes and accounts payable	¥ 3,210	¥ 3,210	¥—
Short-term bank loans	21,957	21,957	—
Accounts payable—other	6,357	6,357	—
Income taxes payable	5,890	5,890	—
Total	¥37,415	¥37,415	¥—
Derivative transactions	¥ 858	¥ 858	¥—
¥ in millions			
2013			
	Carrying value reported in the balance sheet	Fair value	Difference
Cash and time deposits	¥13,793	¥13,793	¥—
Trade notes and accounts receivable	37,199	37,199	—
Investment securities:			
Other securities	19,642	19,642	—
Total	¥70,635	¥70,635	¥—
Trade notes and accounts payable	¥ 2,954	¥ 2,954	¥—
Short-term bank loans	21,957	21,957	—
Accounts payable—other	8,649	8,649	—
Income taxes payable	4,222	4,222	—
Total	¥37,782	¥37,782	¥—
Derivative transactions	¥ 1,593	¥ 1,593	¥—
US\$ in thousands			
2014			
	Carrying value reported in the balance sheet	Fair value	Difference
Cash and time deposits	\$140,357	\$140,357	\$—
Trade notes and accounts receivable	384,310	384,310	—
Investment securities:			
Other securities	152,974	152,974	—
Total	\$677,642	\$677,642	\$—
Trade notes and accounts receivable	\$ 31,190	\$ 31,190	\$—
Short-term bank loans	213,340	213,340	—
Accounts payable—other	61,773	61,773	—
Income taxes payable	57,236	57,236	—
Total	\$363,540	\$363,540	\$—
Derivative transactions	\$ 8,343	\$ 8,343	\$—

FINANCIAL SECTION

Unlisted stocks of ¥98 million (U.S.\$959 thousand) and ¥98 million as of March 31, 2014 and 2013, respectively, whose fair value is extremely difficult to determine were not included in the above table.

Furthermore, unlisted stocks of ¥1,620 million (U.S.\$15,740 thousand) and ¥1,620 million included in "Investments in non-consolidated subsidiaries and affiliates" as of March 31, 2014 and 2013, respectively, whose fair value is extremely difficult to determine were not included in the above table.

The valuation method of fair value of financial instruments and information regarding marketable and investment securities and derivative transactions is summarized as follows.

Cash and time deposits and trade notes and accounts receivable:

The carrying value is deemed as the fair value since these items are scheduled to be settled in a short period of time.

Investment securities:

The fair value of stocks is based on the quoted market prices.

The fair value of bonds is based on the price provided by the counterparty financial institutions. Please refer to Note 3: Investment Securities for information regarding securities by classification.

Trade notes and accounts payable, short-term bank loans, account payable—other, and income taxes payable:

The carrying value is deemed as the fair value since these items are scheduled to be settled in a short period of time.

Derivative transactions:

Please refer to Note 15: Derivatives.

The redemption schedule of monetary assets and securities with maturity dates at March 31, 2014 and 2013, is summarized as follows:

¥ in millions				
2014				
	Within one year	Over one year within five years	Over five years within ten years	Over ten years
Cash and time deposits	¥14,409	¥—	¥—	¥—
Trade notes and accounts receivable	39,553	—	—	—
Total	¥53,963	¥—	¥—	¥—
¥ in millions				
2013				
	Within one year	Over one year within five years	Over five years within ten years	Over ten years
Cash and time deposits	¥13,765	¥—	¥ —	¥—
Trade notes and accounts receivable	37,199	—	—	—
Investment securities				
Other securities with maturity dates (corporate bonds)	—	—	1,000	—
Total	¥50,964	¥—	¥1,000	¥—
US\$ in thousands				
2014				
	Within one year	Over one year within five years	Over five years within ten years	Over ten years
Cash and time deposits	\$140,011	\$—	\$—	\$—
Trade notes and accounts receivable	384,310	—	—	—
Total	\$524,322	\$—	\$—	\$—

The repayment schedule of bonds payable and long-term loans payable after the fiscal year-end:

Please refer to Note 7: Debt.

5 Inventories

Inventories at March 31, 2014 and 2013, consisted of the following:

		¥ in millions	US\$ in thousands
		2014	2013
Merchandise and finished goods	¥ 8,842	¥ 6,862	\$ 85,917
Work in process	10,542	8,351	102,438
Raw materials and supplies	24,038	20,351	233,565
Total	¥43,424	¥35,565	\$421,921

Inventories at March 31, 2014 and 2013, are stated at net selling value. Losses valuation of inventories included in cost of sales were ¥50 million (U.S.\$491 thousand) and ¥127 million for the years ended March 31, 2014 and 2013, respectively.

6 Land Revaluation

In accordance with the Land Revaluation Law (Proclamation No. 34, dated March 31, 1998), land used for business activities was revalued at March 31, 2002. Unrealized revaluation gain on land, net of related deferred taxes, has been presented as a component of net assets.

The market value of the land as of March 31, 2014 and 2013, decreased by ¥2,465 million (U.S.\$23,953 thousand) and by ¥2,363 million after the revaluation, respectively.

7 Debt

Short-term bank loans at average interest rates of 0.8% and 1.0% amounted to ¥21,957 million (U.S.\$213,340 thousand) and ¥21,957 million at March 31, 2014, and April 1, 2013, respectively.

Long-term debt at March 31, 2014, and April 1, 2013, consisted of the following:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Lease obligations, maturing through 2020	¥131	¥102	\$1,276
Less: current portion	(33)	(26)	(321)
	¥ 98	¥ 76	\$ 954

The aggregate annual maturities of lease obligations subsequent to March 31, 2014, are summarized as follows:

Years ending March 31	¥ in millions	US\$ in thousands
2015	¥ 33	\$ 321
2016	31	309
2017	26	258
2018 and thereafter	39	386
Total	¥131	\$1,276

No assets were pledged as collateral for short-term bank loans and long-term debt at March 31, 2014 and 2013.

The Company and its consolidated subsidiaries had no credit commitments with a bank at March 31, 2014 and 2013.

8 Income Taxes

At March 31, 2014 and 2013, the significant components of deferred tax assets and liabilities are summarized as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Deferred tax assets:			
Employees' retirement and severance benefits	¥ —	¥ 737	\$ —
Net defined benefit liability	834	—	8,107
Accrued bonuses	907	952	8,814
Accrued enterprise tax	427	375	4,157
Other	927	753	9,014
Total deferred tax assets	3,097	2,818	30,094
Valuation allowance	(149)	(188)	(1,448)
Deferred tax assets recognized	2,948	2,630	28,646
Deferred tax liabilities:			
Unrealized holding gain on other securities	(924)	(1,800)	(8,982)
Deferred gain on hedges	(306)	(605)	(2,973)
Other	(103)	(62)	(1,002)
Total deferred tax liabilities	(1,333)	(2,468)	(12,958)
Net deferred tax assets	¥ 1,614	¥ 161	\$ 15,687

FINANCIAL SECTION

The Company and its consolidated subsidiaries are subject to a number of taxes based on income which, in the aggregate, resulted in a statutory tax rate of approximately 38.0% for the years ended March 31, 2014 and 2013. The statutory tax rate reflected in the

accompanying consolidated statements of income for the years ended March 31, 2014 and 2013, differs from the effective tax rates for the following reasons:

	2014	2013
Statutory tax rate	38.0%	38.0%
Effect of:		
Inhabitants per capita taxes	0.3	0.4
Permanent differences such as entertainment and donation expenses	0.5	0.7
Nontaxable dividend income	(0.3)	(0.4)
Tax credit for research and development expense	(2.0)	(1.9)
Tax credit for investment in manufacturing facilities	(0.3)	–
Decrease in valuation allowance	(0.1)	(0.2)
Reduction of deferred tax assets due to income tax rate change	0.4	–
Other	(1.3)	(0.9)
Effective tax rates	35.2%	35.7%

The “Act on Partial Revision of the Income Tax Act” was promulgated on March 31, 2014 and the special reconstruction surtax will no longer be imposed from fiscal years beginning on or after April 1, 2014.

Accordingly, the statutory tax rate used to calculate deferred tax assets and deferred tax liabilities was reduced from 38.0% to 35.6% for temporary differences expected to be realized in the fiscal year beginning on April 1, 2014.

As a result, deferred tax assets, net of deferred tax liabilities, decreased by ¥106 million (U.S.\$1,036 thousand), income taxes-deferred and deferred gain (loss) on hedges, net of taxes, increased by ¥119 million (U.S.\$1,164 thousand), and ¥14 million (U.S.\$140 thousand), respectively, and remeasurements of defined benefit plans decreased by ¥1 million (U.S.\$13 thousand) as of and for the year ended March 31, 2014.

9 Employees' Retirement and Severance Benefits

(Fiscal 2014)

The Company maintains a combination plan of funded and unfunded defined benefit plan, defined contribution plan and employees' pension fund plan (multi-employer pension plan).

The Company maintains a cash-balance plan, which is a contract-type corporate pension plan, as a defined benefit corporate pension plan (funded). Under this plan, a hypothetical individual account balance corresponding to each participant's funded amount and the basis of the pension amount is established. An earned interest credit based on market interest rate trends and a point allocation which is determined by the number of service years and employee rank times a unit value for each point, are accumulated in this hypothetical individual account balance.

Under the lump-sum severance payment plan (unfunded), employees who terminate their employment are entitled to lump-sum severance benefits based on their length of service and level of compensation at the time of the termination.

The Company's consolidated subsidiaries maintain a defined benefit corporate pension plan, defined contribution corporate pension plan, and employees' pension fund plan (multi-employer pension plan). The Company's consolidated subsidiaries use the simplified method for the calculation of net defined benefit liability and retirement benefit expenses.

In addition, the Company and its consolidated subsidiaries pay meritorious service awards to employees in excess of the prescribed formula.

The employees' pension fund, in which the Company and its consolidated subsidiaries participate, is a multi-employer type. Since it is difficult to reasonably calculate the Companies' portion of the plan assets corresponding to its contributions, the contributions to the plan assets are recorded as periodic benefit expenses.

(Defined benefit plan)

(1) The changes in retirement and severance benefit obligations for the year ended March 31, 2014, are as follows:

	¥ in millions	US\$ in thousands
Balance at beginning of year	¥15,181	\$147,506
Service cost	703	6,839
Interest cost on benefit obligation	224	2,180
Actuarial gain or loss	(72)	(699)
Benefits paid	(608)	(5,916)
Other	17	170
Balance at end of year	¥15,446	\$150,080

(2) The changes in plan assets for the year ended March 31, 2014, are as follows:

	¥ in millions	US\$ in thousands
Balance at beginning of year	¥11,524	\$111,975
Expected return on plan assets	397	3,866
Actuarial gain or loss	663	6,444
Employer's contribution	1,056	10,266
Benefits paid	(549)	(5,334)
Other	11	112
Balance at end of year	¥13,104	\$127,331

(3) The reconciliation between the liability recorded on the consolidated balance sheet and the balances of retirement and severance benefit obligations and plan assets as of March 31, 2014, is as follows:

	¥ in millions	US\$ in thousands
Funded retirement and severance benefit obligations	¥ 15,414	\$ 149,767
Plan assets	(13,104)	(127,331)
	2,309	22,435
Unfunded retirement and severance benefit obligations	32	313
Net liability for retirement and severance benefit obligations on the consolidated balance sheet	¥ 2,341	\$ 22,749
	¥ in millions	US\$ in thousands
Net defined benefit liability	¥2,341	\$22,749
Net defined benefit asset	—	—
Net defined benefit liability on the consolidated balance sheet	¥2,341	\$22,749

(4) The components of net retirement benefit expenses for the year ended March 31, 2014, are as follows:

	¥ in millions	US\$ in thousands
Service cost	¥ 703	\$ 6,839
Interest cost on benefit obligation	224	2,180
Expected return on plan assets	(397)	(3,866)
Amortization of actuarial gain or loss	269	2,619
Amortization of prior service cost	(96)	(938)
Other	18	175
Net retirement benefit expenses	¥ 721	\$ 7,009

(5) The components of remeasurements of defined benefit plans (before income tax effect) as of March 31, 2014, are as follows:

	¥ in millions	US\$ in thousands
Unrecognized prior service cost	¥ (81)	\$ (792)
Unrecognized actuarial gain or loss	774	7,522
Total	¥ 692	\$6,730

(6) The components of plan assets as of March 31, 2014, are as follows:

Debt securities	27%
Equity securities	40%
General accounts	31%
Other	2%
Total	100%

The expected long-term rate of return on plan assets is determined considering the long-term rates of return, which are expected currently and in the future, from various components of the plan assets.

(7) The assumptions used for the year ended March 31, 2014, are as follows:

Discount rate	1.5%
Expected long-term rate of return on plan assets	3.5%

(8) Simplified method

Plans for which the simplified method is applied are included in the above tables due to their immateriality.

(Defined contribution plan)

The required contribution amount to the defined contribution plan (including the multi-employer employees' pension fund plan accounted for in the same way as the defined contribution plan) is ¥1,029 million (U.S.\$9,999 thousand) for the year ended March 31, 2014.

FINANCIAL SECTION

(The multi-employer plan for which the required contribution amount is recorded as retirement benefit expenses)

(1) Overall funding status as of March 31, 2014, is as follows:

	¥ in millions	US\$ in thousands
Plan assets	¥465,229	\$4,520,304
Benefit obligations, calculated based on assumptions for the entire plans	497,125	4,830,208
Difference	¥ (31,895)	\$ (309,904)

The amounts in the above table are provided based on the most recent available information (as of March 31, 2013, for fiscal 2014).

(2) Contribution ratio of the Company to the entire plans during the year ended March 31, 2014, is 3.78%.

(3) Supplemental information

The difference described in (1) above was calculated by the sum of the balance of the unamortized prior service costs of ¥(49,513) million (U.S.\$(481,087) thousand) and earnings of the fund for this year of ¥17,618 million (U.S.\$171,183 thousand).

The balance of unamortized prior service costs represents the present value of special premium income and is amortized using the straight-line method with a 15.5% premium ratio burdened by the employer. The remaining amortization period is 9 years and 0 months as of March 31, 2013.

The ratio in (2) above is not equal to the actual share ratio.

(Fiscal 2013)

The Company maintains a combination plan of cash-balanced, defined contribution plan and employees' pension fund plan (multi-employer plan).

The Company's domestic subsidiaries maintain an employees' pension fund (multi-employer plan) and a defined benefit corporate pension plan.

Under these plans, employees who terminate their employment are entitled to lump-sum or retirement pension or severance benefits based on their length of service and level of compensation at the time of the termination.

In addition, the Company and its domestic subsidiaries pay meritorious service awards to employees in excess of the prescribed formula, which are charged to income as paid as it is not practicable to compute the liability for such future payments since the amounts vary depending on the circumstances.

(Multi-employer plan)

Required contributions for the multi-employer plan as stated above are included in retirement benefit expenses.

(1) Overall funding status as of March 31, 2013, is as follows:

	¥ in millions
Plan assets	¥414,218
Benefit obligations, calculated based on assumptions for the entire plans	(459,016)
Difference	¥(44,797)

The amounts in the above table are provided based on the most recent available information (as of March 31, 2012, for fiscal 2013).

(2) Contribution ratio of the Company to the entire plans during the year ended March 31, 2013, is 3.68%.

(3) Supplemental information

The difference described in (1) above was calculated by the sum of the balance of the unamortized prior service costs of ¥38,602 million, accumulated deficit of the fund at end of the prior year of ¥3,215 million, and deficit of the fund this year of ¥2,979 million.

The balance of unamortized prior service costs represents the present value of special premium income and is amortized using the straight-line method with a 15.5% premium ratio burdened by the employer. The remaining amortization period is 6 years and 10 months as of March 31, 2012.

The ratio in (2) above is not equal to the actual share ratio.

The following table summarizes the funded status and amounts recognized in the consolidated balance sheet at March 31, 2013:

	¥ in millions
	2013
Retirement and severance benefit obligations	¥(15,181)
Plan assets	11,524
Unfunded benefit obligation	(3,656)
Unrecognized actuarial gain and loss	1,779
Unrecognized prior service cost	(178)
Accrued employees' retirement and severance benefits	¥ (2,055)

The following table summarizes the components of the net retirement benefit expenses for the year ended March 31, 2013:

	¥ in millions
	2013
Service cost	¥1,288
Interest cost on benefit obligation	306
Expected return on plan assets	(346)
Amortization of unrecognized actuarial gain and loss	304
Amortization of unrecognized prior service cost	(62)
Other	342
Net retirement benefit expenses	¥1,832

The assumptions used in determining pension benefit obligation are shown below:

	2013
Method of periodic allocation of estimated retirement benefits	Straight-line method
Discount rate	1.5%
Expected rate of return on assets	3.5%
Amortization period of prior service cost	10 years
Amortization period of actuarial gain and loss	10 years

10 Net Assets

The Companies Act of Japan (the "Act"), which superseded most of the provisions of the Commercial Code of Japan, went into effect on May 1, 2006. The Act provides that an amount equal to 10% of the amount to be disbursed as distributions of capital surplus (other than the capital reserve) and retained earnings (other than the legal reserve) be transferred to the capital reserve and the legal reserve, respectively, until the sum of the capital

reserve and the legal reserve equals 25% of the capital stock account. Such distributions can be made at any time by resolution of the shareholders, or by the Board of Directors if certain conditions are met. The legal reserve amounted to ¥2,649 million (U.S.\$25,743 thousand) and ¥2,198 million as of March 31, 2014 and 2013, respectively.

11 Amounts per Share

Net assets per share as of March 31, 2014 and 2013, are ¥1,860.14 (U.S.\$18.07) and ¥1,658.88, respectively.

Net income per share for the years ended March 31, 2014 and 2013, is ¥255.94 (U.S.\$2.48) and ¥217.98, respectively.

As discussed in Note 1(r), the Company has applied the Accounting Standard for Retirement Benefits and others and has followed the transitional treatment in Article 37 of the standard. As a result, net assets per share decreased by ¥6.32 (U.S.\$0.06) as of March 31, 2014.

The basis for calculation of basic total net assets per share as of March 31, 2014 and 2013, is as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Basic total net assets per share:			
Total net assets	¥133,318	¥118,537	\$1,295,357
Less: Minority interests in consolidated subsidiaries	2,131	1,542	20,705
Amounts attributable to shareholders of common stock	¥131,187	¥116,994	\$1,274,652
Number of shares outstanding at the end of the periods	70,525,381	70,526,265	70,525,381

The basis for calculation of basic net income per share for the years ended March 31, 2014 and 2013, is as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Basic net income per share:			
Net income	¥18,050	¥15,373	\$175,385
Less: Amounts not attributable to shareholders of common stock	—	—	—
Amounts attributable to shareholders of common stock	¥18,050	¥15,373	\$175,385
Weighted-average number of shares outstanding	70,525,823	70,526,550	70,525,823

FINANCIAL SECTION

Basic net income per share is computed based on the net income and the weighted-average number of shares of common stock outstanding during each year. Diluted net income per share is computed based on the net income and the weighted-average number of shares of common stock outstanding during each year after giving effect to the dilutive potential of shares of common stock to be issued. Diluted net income per share for the years ended March 31, 2014 and 2013, has not been presented because

there were no potentially dilutive securities at March 31, 2014 and 2013, respectively.

Net assets per share are based on the number of shares of common stock outstanding at each balance sheet date.

The Company and its consolidated subsidiaries and non-consolidated subsidiaries and other affiliates to which the equity method had been applied had 246,281 and 245,397 shares of treasury stock at March 31, 2014 and 2013, respectively.

12 Major Expenses

Major expenses included in selling, general and administrative expenses for the years ended March 31, 2014 and 2013, are as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Sales promotion expenses	¥ 4,477	¥ 4,213	\$ 43,500
Sales rebates	7,904	7,688	76,802
Salaries and allowances	17,171	16,866	166,844
Research and development expenses	5,949	4,904	57,807
Provision for employees' retirement and severance benefits	1,086	1,186	10,559

Research and development expenses included in general and administrative expenses and cost of sales for the years ended March 31, 2014 and 2013, amounted to ¥5,949 million (U.S.\$57,807 thousand) and ¥4,904 million, respectively.

13 Cash and Cash Equivalents

A reconciliation of cash and cash equivalents at March 31, 2014 and 2013, to the accounts and amounts in the accompanying balance sheets is summarized as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Cash and time deposits	¥14,445	¥13,793	\$140,357
Less: Time deposits with a maturity in excess of three months	(27)	(31)	(262)
Cash and cash equivalents	¥14,418	¥13,762	\$140,094

14 Leases

Finance lease transactions that do not transfer ownership

Leased assets consisted of test facilities in the laboratory, etc.

Finance lease transactions that do not transfer ownership commenced on or before March 31, 2008, are still accounted for in the same manner as operating lease transactions.

Pro-forma information of leased assets such as acquisition cost, accumulated depreciation, obligations under finance leases, depreciation expense, interest expense, and other information of finance leases that do not transfer ownership of the leased assets to the lessee on an "as if capitalized" basis for the years ended March 31, 2014 and 2013, are as follows:

1) A summary of the pro-forma amounts for acquisition cost, accumulated depreciation, and net book value relating primarily to tools, furniture and fixtures at March 31, 2014 and 2013, are as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Acquisition cost	¥61	¥61	\$594
Accumulated depreciation	54	46	533
Net book value	¥ 6	¥14	\$ 61

2) Future minimum lease payments at March 31, 2014 and 2013, are summarized as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Payments in one year or less	¥5	¥ 8	\$57
Payments after one year	0	6	4
Total	¥6	¥14	\$61

3) Lease payments and pro-forma depreciation charges for the years ended March 31, 2014 and 2013, are analyzed as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Lease payments	¥8	¥18	\$84
Pro-forma depreciation charges	8	18	84

4) Depreciation and interest allocation policy

The pro-forma effects of depreciation are computed using the straight-line method over lease terms with no residual value.

Operating leases

Future minimum lease payments for non-cancellable operating leases subsequent to March 31, 2014 and 2013, are as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Payable in one year or less	¥52	¥46	\$505
Payable after one year	30	18	295
Total	¥82	¥65	\$801

15 Derivatives

The Company and its consolidated subsidiaries have entered into foreign exchange forward contracts to reduce its exposure to the risk of future adverse fluctuations in foreign exchange rates related to assets and liabilities denominated in foreign currencies.

An unrealized gain or loss on a hedge instrument is deferred until the Company recognizes a gain or loss on the hedged item.

It is the Company's policy not to enter into any speculative derivatives transactions. The Company and its consolidated subsidiaries have entered into derivative transactions to hedge foreign exchange risk of normal foreign currency transactions based on past import activities, etc.

The management of the Company considers that the Company would not be significantly impacted by market risk related to derivative transactions because their effects on income would be opposite to the effects of the underlying hedged transactions. As the Company enters into contracts with domestic banks with high credit ratings, the Company does not anticipate any risk of non-performance by these counterparties.

The Company and its consolidated subsidiaries enter into and monitor derivative transactions in accordance with internal execution and control regulations relating to derivative transactions, which stipulate control policies, purpose, scope and reporting system of derivative transactions.

FINANCIAL SECTION

Derivative transactions for which hedge accounting has been applied at March 31, 2014 and 2013, are as follows:

Currency related

			¥ in millions			US\$ in thousands		
						2014		
Hedge accounting method	Transaction	Hedged items	Contract amount	Contract amount over one year	Fair value	Contract amount	Contract amount over one year	Fair value
Allocation method	Foreign exchange forward contracts USD (Buying)	Forecast transactions denominated in foreign currency	¥28,101	¥11,639	¥858	\$273,040	\$113,096	\$8,343
			¥ in millions					
			2013					
Hedge accounting method	Transaction	Hedged items	Contract amount	Contract amount over one year	Fair value			
Allocation method	Foreign exchange forward contracts USD (Buying)	Forecast transactions denominated in foreign currency	¥10,949	¥-	¥1,593			

Fair value is principally based on obtaining quotes from counterparty financial institutions.

Information on derivative transactions for which hedge accounting does not apply is omitted since all outstanding derivative positions qualified for hedge accounting.

16 Comprehensive Income

Reclassifications and adjustments and income tax effects attributable to other comprehensive income for the years ended March 31, 2014 and 2013, are as follows:

	¥ in millions		US\$ in thousands
	2014	2013	2014
Unrealized holding gain (loss) on other securities, net of taxes:			
Gains arising during the year	¥ 2,007	¥ 5,325	\$ 19,507
Reclassifications and adjustments	(4,416)	(2)	(42,910)
Before income tax effects	(2,408)	5,322	(23,403)
Income tax effects	875	(1,864)	8,506
Unrealized holding gain (loss) on other securities, net of taxes	¥(1,533)	¥ 3,458	\$(14,896)
Deferred gain (loss) on hedges, net of taxes:			
Gains (losses) arising during the year	¥ (734)	¥ 968	\$ (7,137)
Income tax effects	299	(368)	2,910
Deferred gain (loss) on hedges, net of taxes	¥ (434)	¥ 600	\$ (4,226)
Translation adjustments:			
Adjustments arising during the year	¥ 3,447	¥ 983	\$ 33,497
Translation adjustments	¥ 3,447	¥ 983	\$ 33,497
Share of other comprehensive income of affiliates accounted for using equity method:			
Gains arising during the year	¥ 94	¥ 38	\$ 921
Share of other comprehensive income of affiliates accounted for using equity method	¥ 94	¥ 38	\$ 921
Total other comprehensive income	¥ 1,574	¥ 5,080	\$ 15,296

17 Segment Information

Information about reportable segments is not disclosed since the Company and its consolidated subsidiaries have categorized its reportable segments into a single segment, pharmaceutical products operation.

(Related information)

(1) Information about products and services

Information about products and services is not disclosed since sales amount of single product or service classification to external customers exceeded 90% of net sales on the consolidated statements of income.

(2) Information about geographical areas

(a) Sales

Information about sales by geographical areas is not disclosed since sales to external customers in Japan exceeded 90% of net sales on the consolidated statements of income.

(b) Property, plant and equipment

Information about property, plant and equipment by geographical areas for the years ended March 31, 2014 and 2013, is as follows:

¥ in millions			
2014			
Japan	China	Other	Total
¥45,600	¥11,547	¥0	¥57,148
¥ in millions			
2013			
Japan	China	Other	Total
¥41,176	¥9,480	¥0	¥50,657
US\$ in thousands			
2014			
Japan	China	Other	Total
\$443,065	\$112,197	\$7	\$555,269

(3) Information about major customers for the years ended March 31, 2014 and 2013, is as follows:

Name of major customers	Sales		Segment
	¥ in millions	US\$ in thousands	
		2014	
Alfresa Holdings Corporation	¥28,325	\$275,216	Pharmaceutical products
MEDIPAL HOLDINGS CORPORATION	22,278	216,465	Pharmaceutical products
Suzuken Co., Ltd.	16,926	164,466	Pharmaceutical products
TOHO HOLDINGS CO., LTD.	13,314	129,365	Pharmaceutical products

Name of major customers	Sales		Segment
	¥ in millions		
		2013	
Alfresa Holdings Corporation		¥27,043	Pharmaceutical products
MEDIPAL HOLDINGS CORPORATION		21,262	Pharmaceutical products
Suzuken Co., Ltd.		16,222	Pharmaceutical products
TOHO HOLDINGS CO., LTD.		13,054	Pharmaceutical products

Since the Company and its consolidated subsidiaries have categorized its reportable segments into a single segment, pharmaceutical products operation, information regarding impairment losses on fixed assets by reportable segment for the years ended March 31, 2014 and 2013, was omitted.

18 Impairment Losses

(Fiscal 2014)

For the year ended March 31, 2014, no impairment losses on fixed assets were recognized.

(Fiscal 2013)

For the year ended March 31, 2013, the Company and its consolidated subsidiaries recognized ¥184 million of impairment losses on fixed assets used for business, which consisted of the following:

Location	Description	Classification
Gyoda-shi, Saitama, Japan	Distribution facilities	Buildings, etc.

The Company and its consolidated subsidiaries group their assets used for business on the basis of business segments, considering the characteristics of the products and similarity of markets. Idle assets and assets to be disposed of are grouped individually. The recoverable amount utilized in the calculation was value in use. Discount rates are considered to be immaterial and are not taken into account since the assets are scheduled to be disposed of in a short period of time.

The Company disposed of assets related to distribution facilities and their carrying values have been reduced to their recoverable amounts and recognized in other income (expenses) as impairment losses.

Impairment losses of ¥184 million consist of ¥182 million for buildings and structures etc. for the year ended March 31, 2013.

19 Note to Consolidated Statements of Changes in Net Assets

Issued stock and treasury stock as of March 31, 2014, are as follows:

Number of issued shares

Common stock 70,771,662 shares

The number of treasury stock is as follows:

	At April 1, 2013	Increase	Decrease	Shares At March 31, 2014
Common stock	245,397	884	—	246,281

Dividends from surplus as of March 31, 2014, are as follows:

(1) Dividend payments

Scheduled resolution	Category	Total amount of dividends (¥ in millions)	Dividend per share (¥)	Total amount of dividends (US\$ in thousands)	Dividend per share (US\$)	Record date	Effective date
Ordinary general meeting of shareholders held on June 27, 2013	Common Stock	¥2,256	¥32	\$21,928	\$0.31	March 31, 2013	June 28, 2013
Board of directors' meeting held on November 7, 2013	Common Stock	2,256	32	21,927	0.31	September 30, 2013	December 4, 2013

(2) Dividends whose effective date is subsequent to March 31, 2014

Scheduled resolution	Category	Source of dividends	Total amount of dividends (¥ in millions)	Dividend per share (¥)	Total amount of dividends (US\$ in thousands)	Dividend per share (US\$)	Record date	Effective date
Ordinary general meeting of shareholders held on June 27, 2014	Common Stock	Retained earnings	¥2,256	¥32	\$21,927	\$0.31	March 31, 2014	June 30, 2014

20 Subsequent Event

(1) At the shareholders' meeting held on June 27, 2014, the following appropriation from unappropriated retained earnings of the Company was approved by the shareholders:

	¥ in millions	US\$ in thousands
Cash dividends, ¥32.00 (U.S.\$0.31) per share	¥2,256	\$21,927

(2) Significant borrowings

Based on the resolution at the Board of Directors' meeting held on May 12, 2014, the Company entered into loan agreements with banks for financing capital expenditures and to use as operating funds as follows:

(i) Lenders

The Bank of Tokyo-Mitsubishi UFJ, Ltd., SUMITOMO MITSUI BANKING CORPORATION, Mizuho Bank, Ltd., Mitsubishi UFJ Trust and Banking Corporation, The SHIGA BANK, Ltd., The Hachijuni Bank, Ltd., and The Shizuoka Bank, Ltd.

(ii) Aggregate amount of borrowings
¥15,000 million (U.S.\$145,744 thousand)

(iii) Interest rate
Basic interest rate plus spread

(iv) Execution dates
June 20 and 27, 2014

(v) Repayment method
Lump-sum repayment in four years

(vi) Pledged assets
None

Report of Independent Auditors



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Hibiya Kokusai Bldg.
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Tokyo, Japan 100-0011

Tel: +81 3 3503 1100
Fax: +81 3 3503 1197
www.shinnihon.or.jp

Independent Auditor's Report

The Board of Directors
TSUMURA & CO.

We have audited the accompanying consolidated financial statements of TSUMURA & CO. and its consolidated subsidiaries, which comprise the consolidated balance sheet as at March 31, 2014, and the consolidated statements of income, comprehensive income, changes in net assets, and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information, all expressed in Japanese yen.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in Japan, and for designing and operating such internal control as management determines is necessary to enable the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. The purpose of an audit of the consolidated financial statements is not to express an opinion on the effectiveness of the entity's internal control, but in making these risk assessments the auditor considers internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of TSUMURA & CO. and its consolidated subsidiaries as at March 31, 2014, and their consolidated financial performance and cash flows for the year then ended in conformity with accounting principles generally accepted in Japan.

Convenience Translation

We have reviewed the translation of these consolidated financial statements into U.S. dollars, presented for the convenience of readers, and, in our opinion, the accompanying consolidated financial statements have been properly translated on the basis described in Note 2.

Ernst & Young ShinNihon LLC

June 27, 2014
Tokyo, Japan

Corporate Data

As of March 31, 2014

Head Office: 17-11, Akasaka 2-chome,
Minato-ku, Tokyo 107-8521, Japan
Corporate Communications Department
Phone: 81-3-6361-7101
Fax: 81-3-5574-6630
URL: <http://www.tsumura.co.jp/english/>

Founded: April 10, 1893
Incorporated: April 25, 1936
Number of Employees: 2,898 (Consolidated)
Plants: Shizuoka, Ibaraki, Shanghai
Research Laboratory: Ibaraki

Subsidiaries and Affiliates:

Country	Company	Business
Japan	LOGITEM TSUMURA CO., LTD.	Logistics, storage, distribution, and materials handling services
	CREATIVE SERVICE, INC.	Sales of Kampo products
United States	TSUMURA USA, INC.	Development of pharmaceutical products in the United States
China	SHENZHEN TSUMURA MEDICINE CO., LTD.	Procurement, sorting, processing, and storage of botanical raw materials
	SHANGHAI TSUMURA PHARMACEUTICALS CO., LTD.	Production and sale of Kampo extract intermediates
	SICHUAN CHUANCUN TRADITIONAL CHINESE MEDICINES CO., LTD.	Procurement and sorting of botanical raw materials

Investor Information

As of March 31, 2014

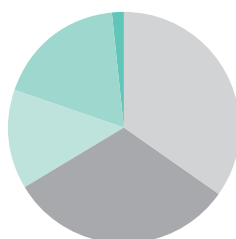
Stock Exchange Listing: Tokyo
Stock Code: 4540
Paid-in Capital: ¥19,487 million
Net Assets: ¥133,318 million
Common Stock:
Authorized: 250,000,000
Issued: 70,771,662
Closing Date of Accounts: March 31
Independent Auditor:
Ernst & Young ShinNihon LLC
Hibiya Kokusai Bldg.,
2-3, Uchisaiwai-cho 2-chome,
Chiyoda-ku, Tokyo 100-0011, Japan
Shareholder Register Agent for Common Stock in Japan:
Mitsubishi UFJ Trust and Banking Corporation
4-5, Marunouchi 1-chome,
Chiyoda-ku, Tokyo 100-8212, Japan
Number of Shareholders: 17,265

Major Shareholders

	% of equity
Japan Trustee Services Bank, Ltd. (Trust Account)	5.83
The Master Trust Bank of Japan, Ltd. (Trust Account)	5.38
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	3.12
Employees' Stockholding	2.69
SAJAP	2.49
DAIICHI SANKYO COMPANY, LIMITED	2.16
National Mutual Insurance Federation of Agricultural Cooperatives	2.13
Japan Trustee Services Bank, Ltd. (Trust Account 9)	2.03
BNYML-NON TREATY ACCOUNT	1.67
Dainippon Sumitomo Pharma Co., Ltd.	1.55

Ownership and Distribution of Shares

%



Japanese financial institutions	34.78%
Foreign institutions	31.76%
Other Japanese corporations	13.82%
Japanese individuals and others	18.24%
Japanese securities firms	1.40%

TSUMURA & CO.

2-17-11, Akasaka, Minato-ku, Tokyo 107-8521, Japan



Printed in Japan